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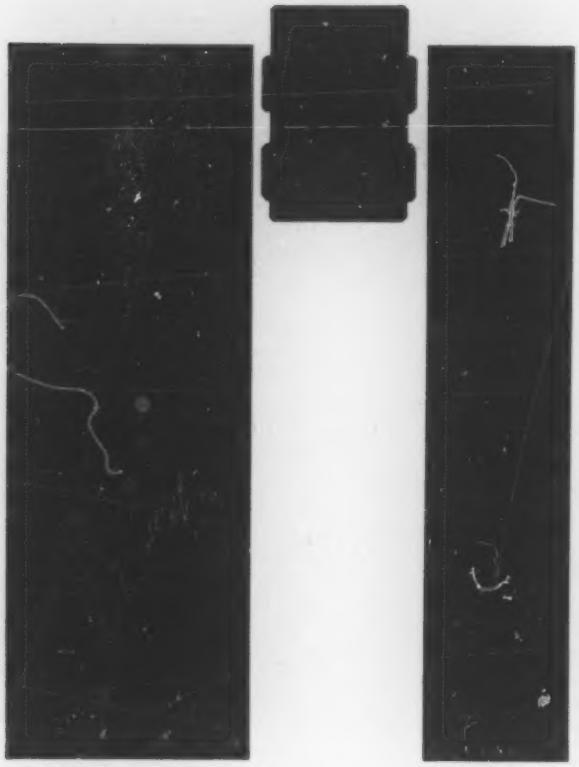
TRENDS IN AUTOMOBILE FINANCING

RESULTS OF THE 1987 SURVEY



CBA
CONSUMER BANKERS ASSOCIATION

1300 NORTH SEVENTEENTH STREET
ARLINGTON, VIRGINIA 22209 • 703/276-1750

Consumer Bankers Association

The Consumer Bankers Association was founded in 1919 to provide a progressive voice for the retail banking industry. CBA represents approximately 700 federally insured banks, savings and loans and credit unions that hold more than 80 percent of all consumer deposits, and more than 70 percent of all consumer credit held by commercial institutions.

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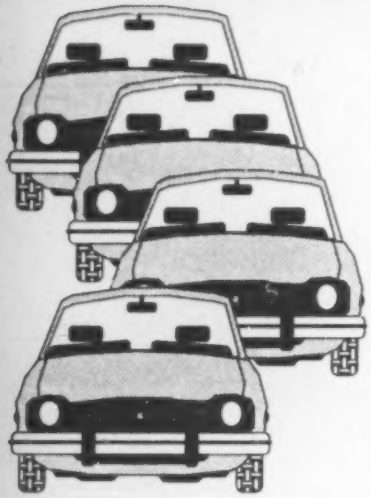

CONSUMER BANKERS
ASSOCIATION

TRENDS IN AUTOMOBILE FINANCING SURVEY

YEAR END 1987

Conducted by the

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CONSUMER BANKERS ASSOCIATION
TRENDS IN AUTOMOBILE FINANCING SURVEY
YEAR END 1987

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Introduction

With the unstable international capital markets, and businesses developing financing alternatives to commercial credit, consumer lending tends to be the fastest growing portion of a financial institution's lending portfolio. Most of this growth is in automobile paper, the volume of which has increased 100% in the last ten years. Automobile loans currently account for over $250 billion, or two-fifths of non-mortgage installment debt, the single largest category of consumer installment credit.

In the late 1970's new car sales totaled almost 11 million units per year, and auto credit expanded at rates approaching 20% annually. By 1982, new cars sales had fallen to a 20 year record low of 8 million, and commercial banks cut back consumer lending. At this same time, the auto makers became aggressive in an effort to sell their cars, and stepped up their efforts in auto financing. They began first by simply making credit available to those who could not obtain it elsewhere. Then they began to offer loans at below market rates. By 1983, the captive finance companies had increased their auto credit holdings to over $20 billion, an increase of over 80% in three years.

In 1983, commercial banks returned to the auto credit market as aggressive competitors. The captive finance companies' support of the market from 1980 to 1983 had strained their balance sheets, so they reduced their participation, phasing out reduced rate financing. In 1984 and 1985 banks eagerly supplied car buyers with credit as the auto market continued to thrive, and in 1985 the captives again entered the market with reduced rate financing. There is a two-way causal relationship between auto sales and credit terms, as the decision to buy a car stimulates demand for loans, while the terms and availability of credit affect the sales of cars. In 1986, automobile sales peaked at over 11 million units. The net result in terms of lending market share in the decade prior to 1987 was a 100% increase by the captives and a 30% decrease by banks, to the point where they both now control approximately 40% of the new car market.

In 1987, auto sales decreased to just over 10 million units. Predictions for the 1988 new car market vary substantially, but the consensus of experts would suggest that there will be little, if any, improvement in sales in 1988. The possible reasons for the lack of growth are many. Auto sales are cyclical, and some experts contend that demand for autos will continue at lower rates until 1990. There is evidence suggesting that public responsiveness to financing incentives is waning. There is also the growth in the automobile leasing business.

In 1987, 2 million new cars were leased, and some regional markets thrived. In California, one-third of all luxury cars were leased. Comparing the average value of a lease to the average new car loan, the figures would suggest that two markets may be developing, one for the sale of lower priced cars, one for leasing more expensive cars. There are many reasons that leasing is attractive, from both the business and personal perspective, and the effects of the Tax Reform Act of 1986 on leasing may just be beginning to appear.

There was a large variance in the performances of financial institutions in 1987; some fared very well in auto lending and leasing, while others did quite poorly. It would appear as if some institutions are learning what their customers are looking for as well as how to compete with the captives, while others are not. With major demographic changes, changing consumer tastes and preferences, rapidly changing technology, and potential foreign competition in the auto financing business, financial institutions are also going to have to change to be successful. Some large institutions have focused on growth through merger and acquisition, attempting to attain economies of scale, while some smaller institutions have focused on increasing the level of service. One thing seems apparent, that the only constant is change, and the best way to cope with change is to be aware. It is hoped that the information contained in this report will be of use to auto lending and leasing financial executives in 1988.

Survey Response

The 1987 Auto Leasing and Financing survey was distributed to 605 Consumer Bankers Association member institutions, including commercial banks, thrifts, and financial subsidiaries. The response rate was considerably higher than in previous years, with a total of 159 completed surveys received in time to be included in the analysis. This represents an increase of 34% over 1986, an increase that provides two benefits for CBA members. First, it gives a broader base from which to allow comparisons and observe trends in automobile leasing and financing. Second, it permits more confidence to be taken in the results, as greater participation improves accuracy.

Due to the increase in responses, this year the data that have been collected can be stratified to a greater extent than in previous years. Where possible, the results will be broken down by bank asset size and geographic location. This can only be done when there are sufficient numbers of responses to provide a certain degree of confidence in the results. Throughout this report, an effort has been made to highlight the differences that may exist across size and region through the use of tables and graphs. When looking at questions that generated few significant differences, only overall results will be discussed in the text. The geographic breakdown is presented below in Table 1:

GEOGRAPHIC BREAKDOWN

West (W):	AK, CA, CO, HI, ID, MT, NV, OR, UT, WA, WY
Southwest (SW):	AZ, NM, TX, OK
Midwest (MW):	AR, IA, IL, IN, KS, KY, MI, MN, MO, ND, NE, OH, SD, WI
Southeast (SE):	AL, FL, GA, LA, MS, NC, SC, TN
Mid-Atlantic (MA):	DC, DE, MD, NJ, PA, VA
Northeast (NE):	CT, MA, ME, NH, NY, RI, VT

Table 1

Due to low response rates, the central plains region was combined with the midwest, and the rocky mountain region was combined with the pacific coast region to become the west. Combining the regions had very little effect on distorting results for any of the regions involved. Similarly, financial institutions were collapsed into three size categories, those with assets in excess of $5 Billion, those with assets of between $1 Billion and $5 Billion, and those with assets of less than $1 Billion.

While reading this report and examining the graphics, there are several issues to keep in mind. First, the numbers that are presented are the averages for the variable being discussed. In cases where there there were extreme deviations from the average, the responses were deleted from the analysis to provide the most representative results possible. Second, the response rate varied greatly from question to question, and even within different parts of the same question, and some questions permitted more than one response. For these reasons, in some cases totals do not add up to 100%, and numbers may vary slightly in different sections of the report. This is not an error, but is a reflection of the data as collected. Third, when conducting a survey it is always best, but not always possible, to have a random sample. While this report may not be representative of the total U.S. market it accurately reflects the responses of CBA members. It is important to keep in mind that these results reflect the responses of the participants only, and not the entire CBA membership.

General Information

There was a significant amount of diversity in the respondents for 1987, which allowed the data that were collected to be stratified for better comparisons. Table 2 provides a breakdown of respondents by asset size and geographic location, a breakdown which will be continued where appropriate throughout the report.

COMPARISON OF NUMBER OF RESPONDENTS BY INSTITUTION

ASSET SIZE AND GEOGRAPHIC LOCATION

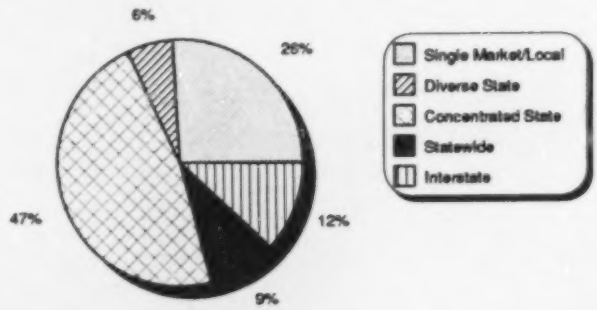
	Asset Size			
Region	Under $1B	$1B-$5B	Over $5B	Total
West	3	7	13	23
Southwest	5	2	5	12
Midwest	14	15	9	38
Southeast	6	15	11	32
Mid-Atlantic	7	20	15	42
Northeast	3	5	4	12
TOTAL	38	64	57	159

Table 2

Of those responding, 24% were from institutions with assets of less than $1 Billion, 40% have assets between $1 Billion and $5 Billion, and 36% have assets in excess of $5 Billion. These percentages, along with those from the geographic breakdown, are very consistent with the 1986 survey. In 1987 single bank holding companies made up 12% of the sample, multi-bank holding companies 50%, independent banks 14%, mutual savings banks 3%, savings and loans 7%, and other organizations 13%. The geographic distribution of institution facilities and assets varied considerably across size and region. The size differences are pointed out in Figures 1 through 3.

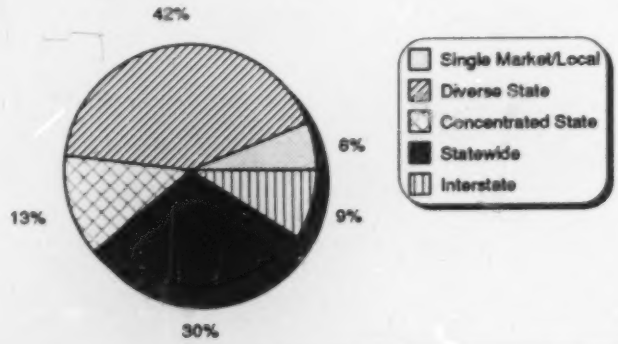
GEOGRAPHIC DISTRIBUTION
Under $1 Billion Institutions

Figure 1



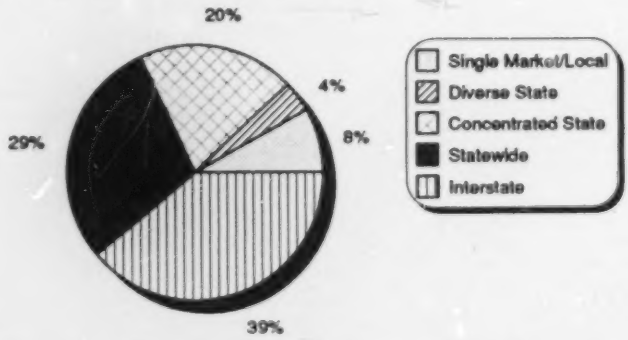
GEOGRAPHIC DISTRIBUTION
$1B - $5B Institutions

Figure 2



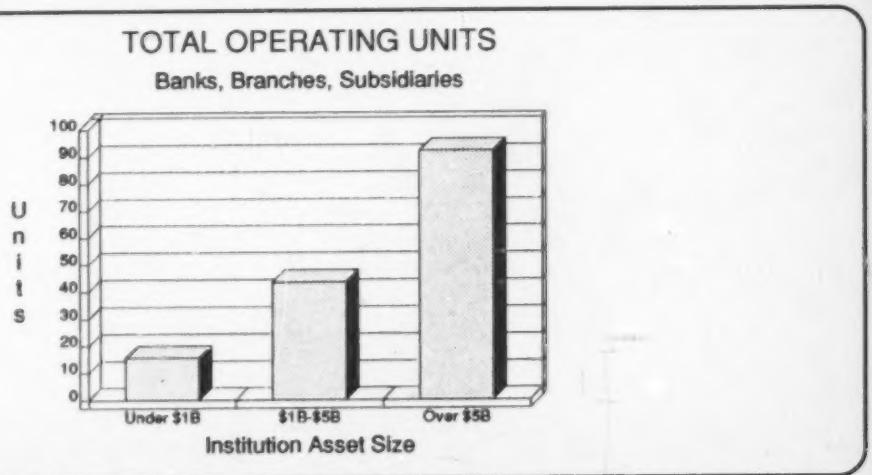
GEOGRAPHIC DISTRIBUTION
Over $5 Billion Institutions

Figure 3



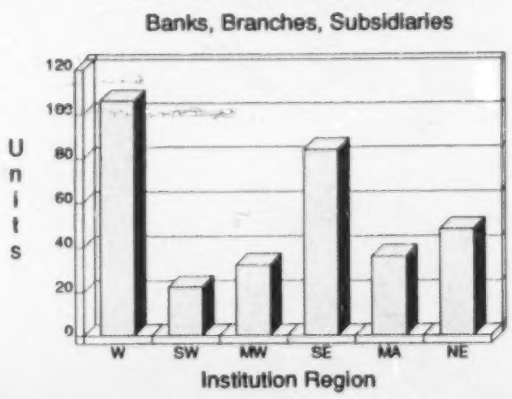
These figures suggest that larger banks are conducting business on a statewide and interstate basis much more commonly than those smaller. Regional differences also exist, as 71% of the institutions in the west (W) described themselves as statewide or interstate, 45% of southwest (SW) was single market, and 51% of the midwest (MW) was concentrated state regional. The other three regions did not demonstrate one dominant distribution pattern. These results are similar to those of prior years, and reflect regulatory differences which exist from region to region. Overall institution size, measured by number of banks, branches, and subsidiaries also varied consistently with asset size and varied regionally, as illustrated in Figures 4 and 5.

Figure 4



The number of units increases in the west (W), where statewide and interstate banking is more common. The average number of total operating units is also large in the southeast (SE) even though interstate banks make up only 16% of the institutions in this region.

Figure 5



Leasing and lending activity vary considerably by institution size and region. These differences are pointed out in Table 3.

PERCENTAGE OF RESPONDENTS ENGAGED

IN LEASING AND LENDING ACTIVITY

Asset Size

	<$1B	1B-5B	>$5B
Leasing & Lending	26%	39%	67%
Lending Only	74%	61%	33%

Regions

	W	SW	MW	SE	MA	NE
Leasing & Lending	56%	36%	57%	35%	42%	60%
Lending Only	44%	64%	43%	65%	58%	40%

Table 3

As these numbers demonstrate, as bank size increases, an institution is much more likely to get involved in leasing activities. Overall, the numbers by asset size show very little change from the 1986 survey with the exception of those institutions with assets of less than $1 Billion. The percentage of those offering both leasing and lending decreased from 36% for this category. Regionally, the numbers are consistent with those of 1986 except for the west (W), which experienced a decrease of 10% for leasing and lending , while the midwest (MW) had an increase of 9% in this category. These results should be interpreted with caution, however, as the overall number of respondents increased by 41 while respondents offering leasing increased only by 6, which may alter percentages.

The average portfolio of loans and leases in 1987 consisted of 30,217 units financed at a value of $195 Million, with 7,392 leases at a value of $90 Million. The average total portfolio consisted of 33,854 units at a dollar value of $241 Million. The number of automobiles leased and financed and the dollar outstandings generated by these leases and loans is presented by institution size and geographic region in Figures 6 through 9.

Figure 6

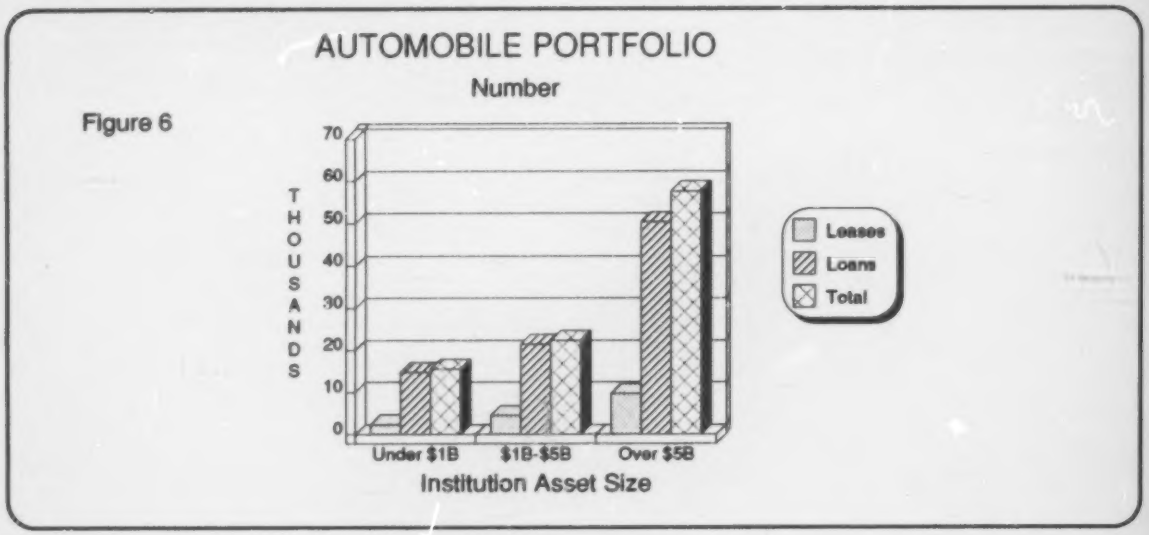
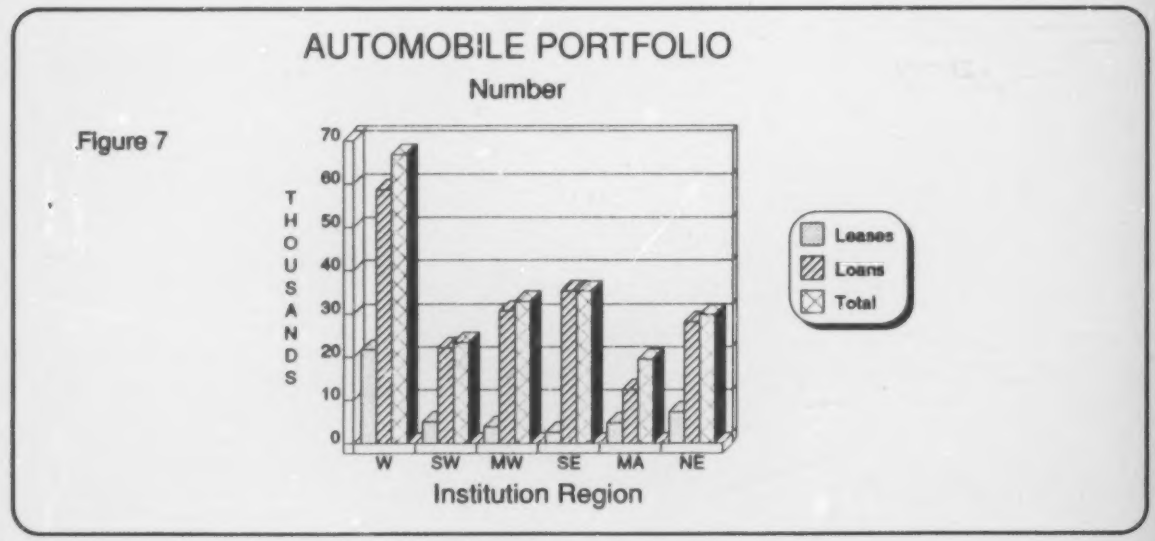


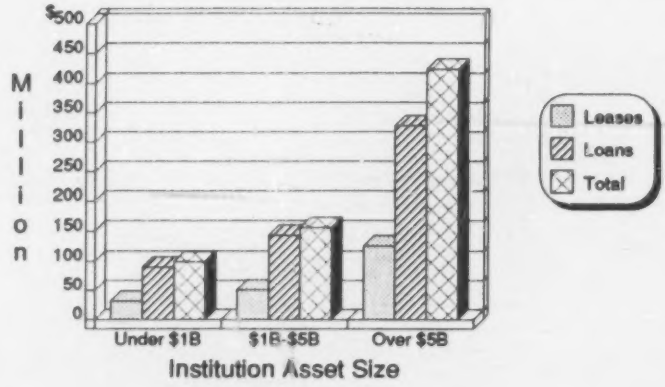
Figure 7



AUTOMOBILE PORTFOLIO

Volume

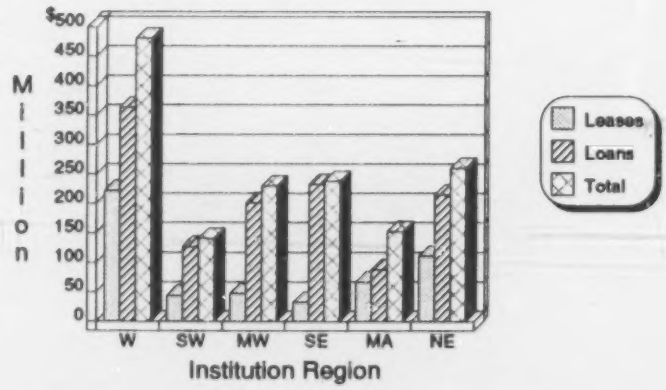
Figure 8



AUTOMOBILE PORTFOLIO

Volume

Figure 9



It is clear that the number of automobiles and the dollar volume in the portfolio increase as institution asset size increases. It is also apparent that regional differences in portfolios exist that cannot be entirely explained by differences in institution size. For example, the average number of leases for western (W) institutions is 21,682, almost three times as large as any other region in the country, with the northeast (NE) a distant second at 7,338. Institutions with assets of less than $1 Billion comprised 37% (see Table 2) of respondents from the midwest (MW), the greatest percentage of small banks in any region, yet they have the third largest average number in the total portfolio at 32,993. The mid-Atlantic institutions have the most large

banks responding, yet are fifth in number of leases and fourth in outstandings of automobile loans and leases. It appears that some banks are generating more leasing and lending activity per asset dollar than others. The results of the 1987 survey show that the value of the average loan in a portfolio is $6,757, compared to $6,460 in 1986 and $7,208 in 1985. The average lease is $12,389, and the average combined total is $7,436.

There are four basic ways in which institutions are organized to handle their leasing and lending activities. These include separate leasing, separate lending, combined leasing and lending, and consolidated, usually in a consumer finance unit. These types are shown in Figures 10 and 11 by asset size and region.

Figure 10

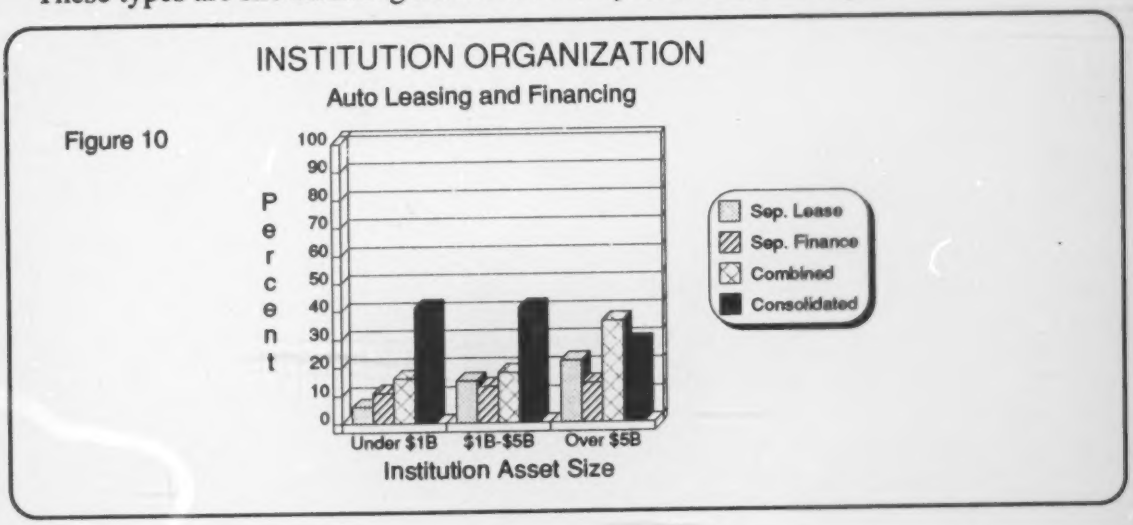
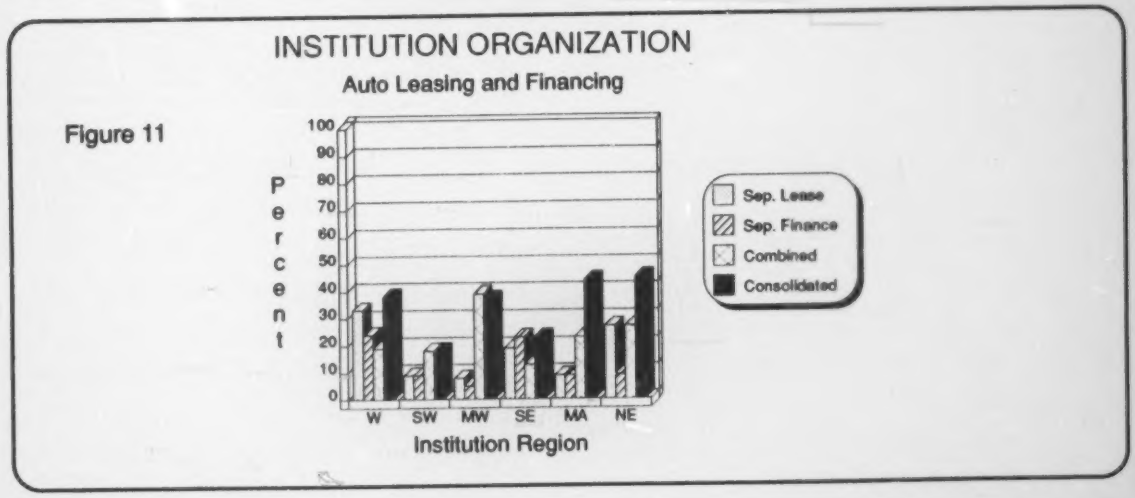


Figure 11



Over 40% of institutions with assets of less that $5 Billion consolidate leasing and lending activities, while 27% of those banks with assets in excess of $5 Billion consolidate. Conversely, the larger banks are more likely to have a separate leasing and financing department, or more commonly (36%) combine the two units. Regional differences also emerge in organization, with institutions in the west (W) and northeast (NE) frequently using separate leasing departments, the midwest (MW) institutions most frequently combining the two departments.

Over 84% of institutions surveyed conduct much of their business with franchise dealers, and an average of 23% have leasing relationships with lease brokers. Figures 12 and 13 illustrate the percentage of institutions that conduct business with lease brokers and franchise dealers, as well as the percentage of the portfolio that is the result of this activity.

Figure 12

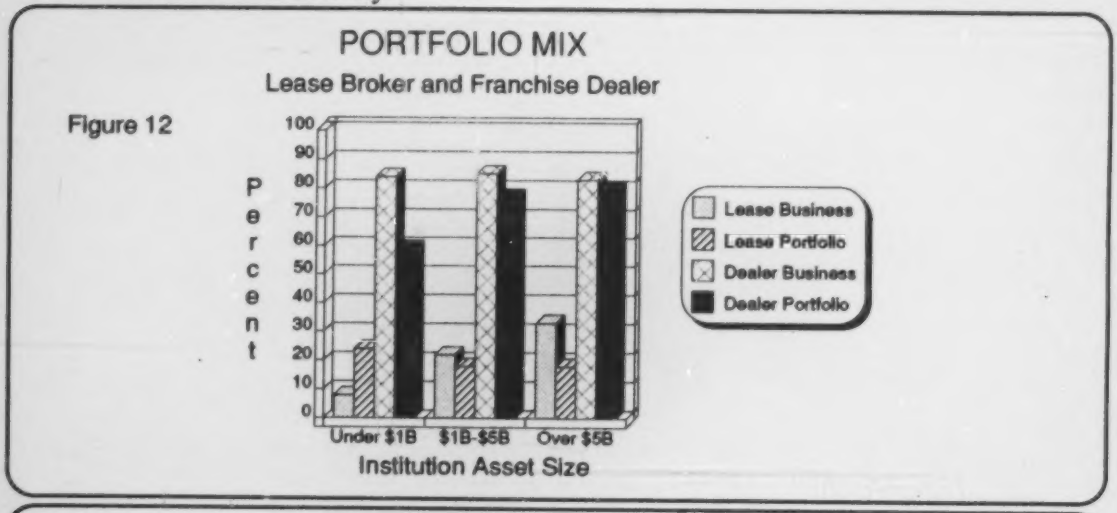
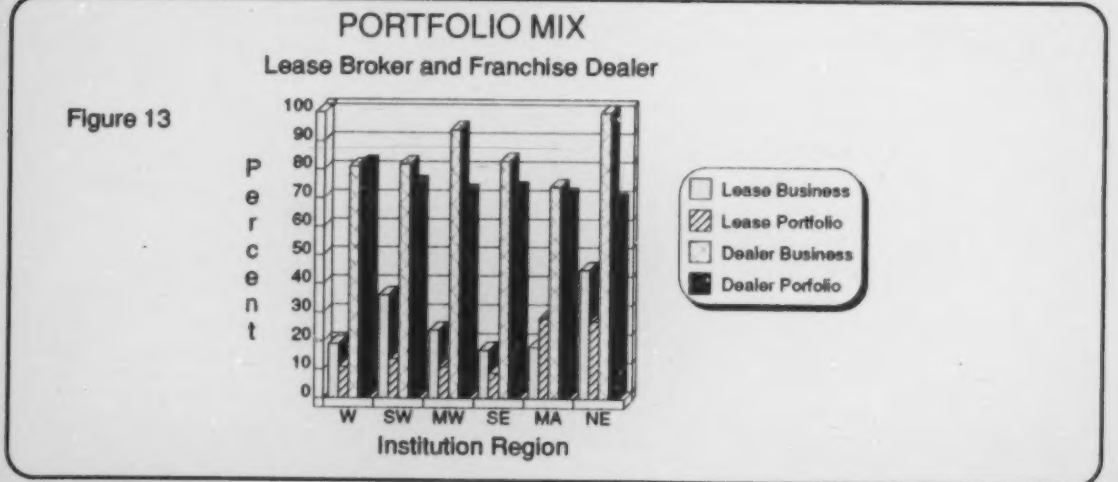


Figure 13



Larger institutions tend to establish relationships more commonly with lease brokers. Institutions with assets of less than $1 Billion have less than 60% of their portfolio from franchise dealers. Regionally, northeastern (NE) and southwestern (SW) institutions establish relationships with lease brokers much more frequently than the rest of the country.

Respondents were asked to provide what they felt was a description of their institution's plans regarding leasing and lending programs for 1988. A summary of the reponses is provided in Table 4:

INSTITUTION PLANS FOR 1988

Future Plans to OFFER programs.

22%	Prepared to implement both auto lending/leasing programs.
6%	Prepared to implement auto leasing program only.
32%	Prepared to implement auto lending program only.
7%	Considered both lending/leasing programs, no immediate plans.
1%	Considered lending program only, no immediate plans.
31%	Considered leasing services, no immediate plans.
1%	No consideration has been given to either leasing or lending.

Future plans to DROP programs.

5%	Considering dropping auto leasing program in near future.
1%	Considering dropping auto lending program in near future.
94%	Will maintain current programs on both lending/leasing.

Future plans to MAINTAIN current programs.

45%	Expect both leasing/lending programs to increase.
1%	Expect only auto leasing program will increase.
32%	Expect only auto lending program will increase.
1%	Expect a decrease in auto leasing only.
7%	Expect a decrease in auto lending only.
14%	Expect no substantial change.

Table 4

Overall, the results suggest that the respondents are optimistic about the coming year, as 45% anticipate an increase in both leasing and lending programs, and only 7% expect a decrease in auto lending. With regard to the future, almost one-third of the respondents are considering offering a leasing program, though they have no immediate plans.

Conclusion

Greater participation in the 1987 CBA Survey has provided a large amount of data to process, providing useful information for CBA members. Increased participation in the future can further serve the needs of the membership. Of particular interest are trends in automobile leasing, the purpose for which the survey was originally developed. In 1987, fully two thirds of the respondents with assets in excess of $5 Billion were involved with leasing. Currently, the leasing centers are in the West (W), Midwest (MW), and Northeast (NE), however, almost one third of all respondents not currently involved in leasing are considering offering leasing services in the future.

Automobile Leasing

The growth in the number of participants in the leasing business continued in 1987, as 67 financial institutions that offered automobile leasing responded to the survey, an increase of almost 10% over 1986. The average age of leasing programs is 7 years, and half of the respondents have been in the leasing business for less than 5 years.

Table 5 provides a breakdown of respondents who offered leasing by asset size and geographic location:

COMPARISON OF NUMBER OF LEASING RESPONDENTS BY INSTITUTION ASSET SIZE AND GEOGRAPHIC LOCATION

	Asset Size			
Region	Under $1B	$1B-$5B	Over $5B	Total
West	0	2	8	10
Southwest	1	2	3	6
Midwest	5	10	5	20
Southeast	1	2	12	15
Mid-Atlantic	1	4	4	9
Northeast	1	3	3	7
TOTAL	9	23	35	67

Table 5

Of those responding, 13% were from institutions with assets of less than $1 Billion, 35% have assets between $1 Billion and $5 Billion, and 52% have assets in excess of $5 Billion. Regionally, the west (W), midwest (MW), and southeast (SE), together comprise over two thirds of total leasing respondents.

The Lease Portfolio

The average leasing portfolio of gross outstandings varied considerably by institution size and geographic region and is presented in Figures 14-15.

Figure 14

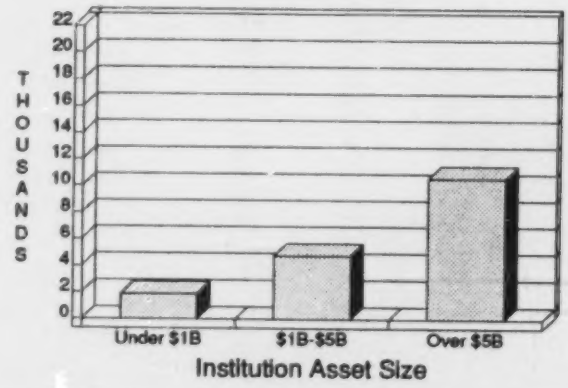
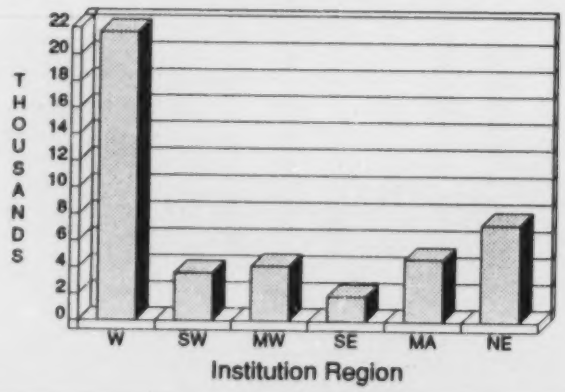


Figure 15



It is clear that as the institution size increases, the total number of leases also increases. Regionally, those institutions in the west (W) greatly exceed the rest of the country in the number and dollar volume of their leasing programs, followed by the northeast (NE). The overall average dollar value per lease in the 1987 portfolio was

$12,389. In terms of the mix of closed-end and open-end leases, the average portfolio was comprised of 81% closed-end leases. The types of leasing programs offered by financial institutions are presented by institution asset size and geographic region in Figures 16-17:

Figure 16

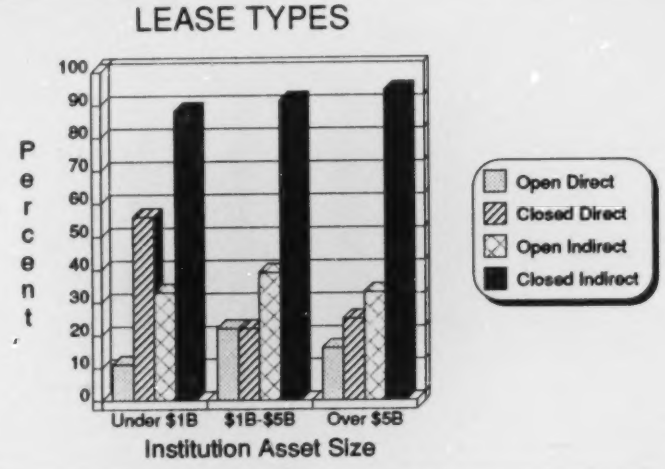
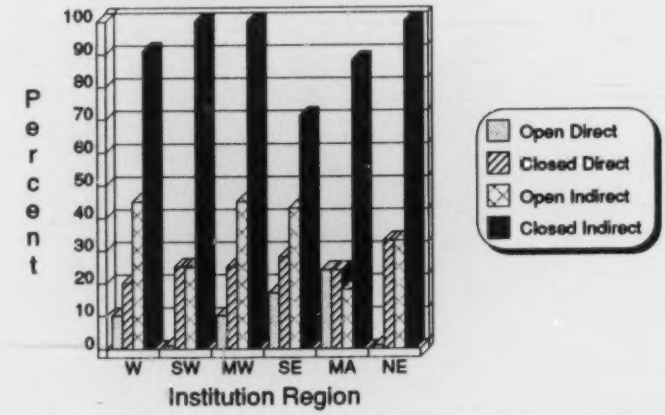


Figure 17



A greater percentage of those institutions with assets of less than $1 Billion tended to offer direct leasing than was offered by the larger institutions. Regionally, the closed-end indirect lease is by far the most common offering.

Employees

The 1987 survey contained items pertaining to the number of employees involved in the leasing function, as well as the salaries for these employees. Figures 18-21 present the results of the survey:

Figure 18

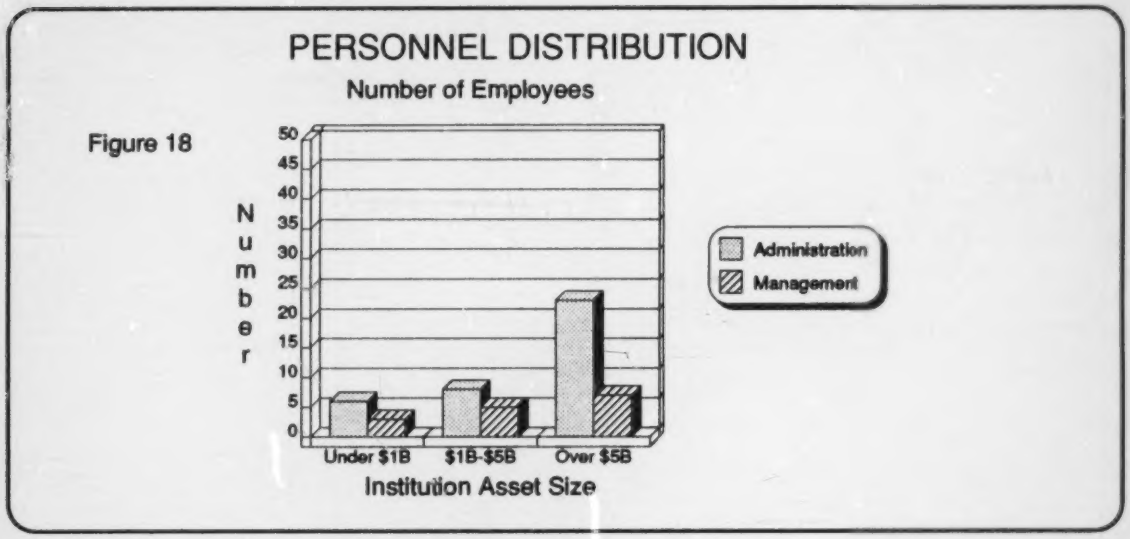


Figure 19

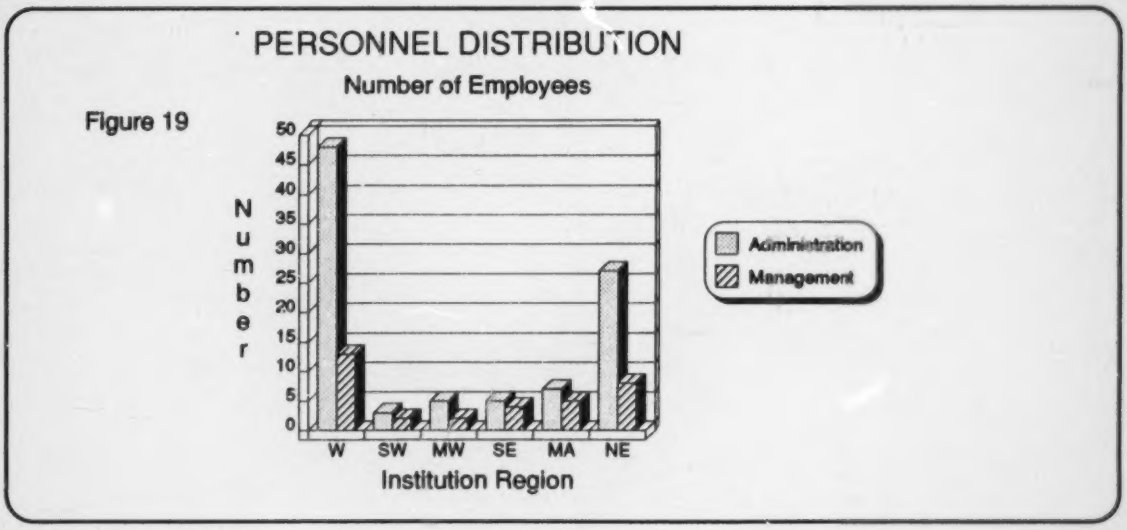


Figure 20

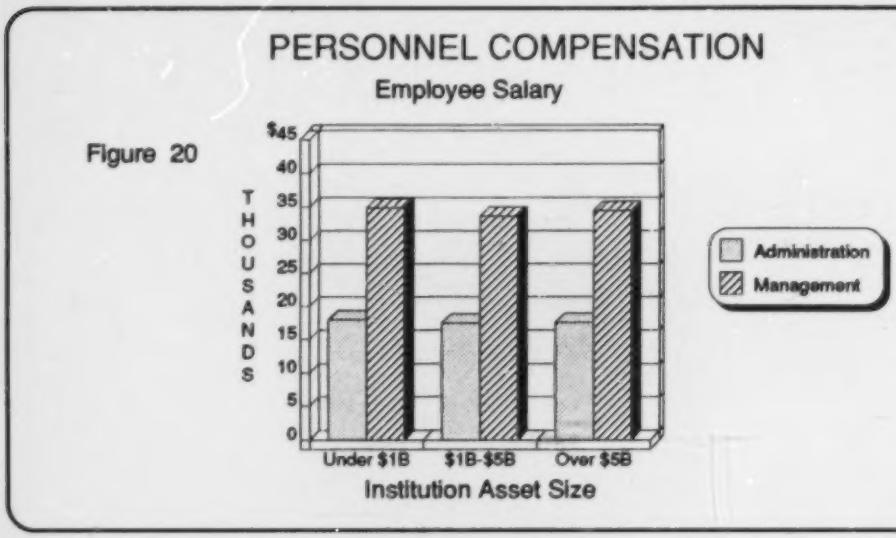
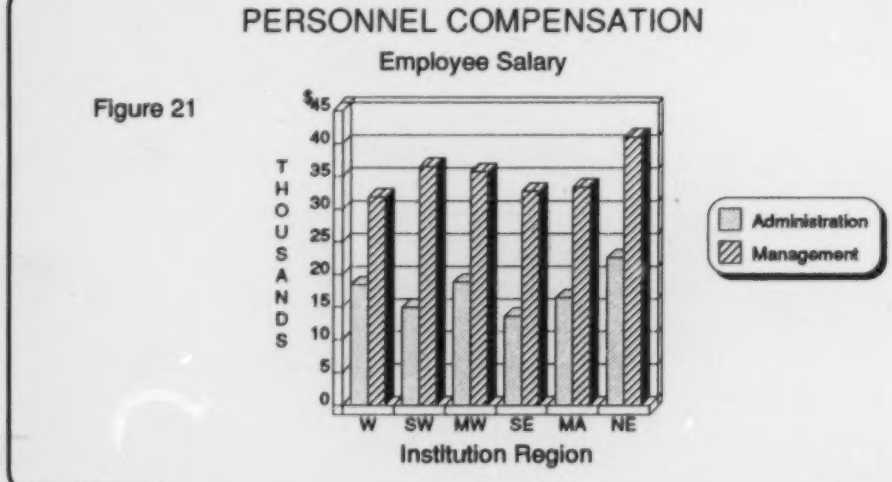


Figure 21



As expected, the larger institutions employ more individuals, but the ratio of managerial employees to administrative personnel decreases with size. Over one third of the number of total employees are classified as managers (exempt) for those institutions with assets of less than $1 Billion, while 24% are classified as managers by the institutions with assets in excess of $5 Billion. Salaries vary little by institution asset size, but do show some regional differences, with higher average salaries in the northeast (NE).

Leasing Activity

There was a substantial degree of optimism expressed in the 1986 survey regarding expectations for 1987. For many organizations, the optimism was justified. There was, however, a great deal of difference among the performance of leasing programs in 1987, as 34% of respondents reported an increase in leasing volume, while 34% reported a decrease, and 32% reported no change. This is an improvement over the figures from 1986, when 65% of respondents reported a decrease in leasing activity. For those who gained, the average increase in the number of leases was 49%, ranging from 7% to 100%. For those institutions reporting a decrease, this average was -39%, with a range from -30% to -72% for the number of leases. Figures 22-23 present the breakdown of changes in lease activity by institution asset size and geographic region:

Figure 22

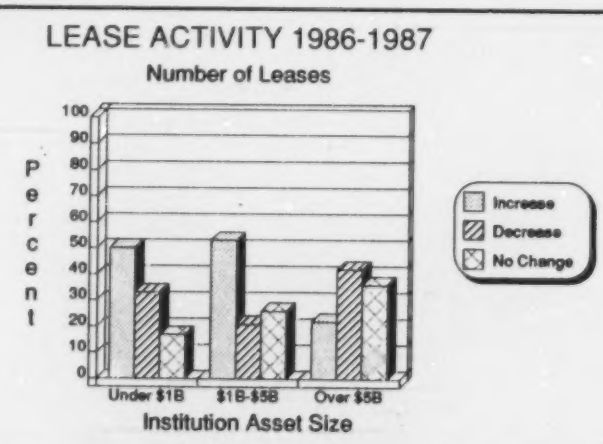
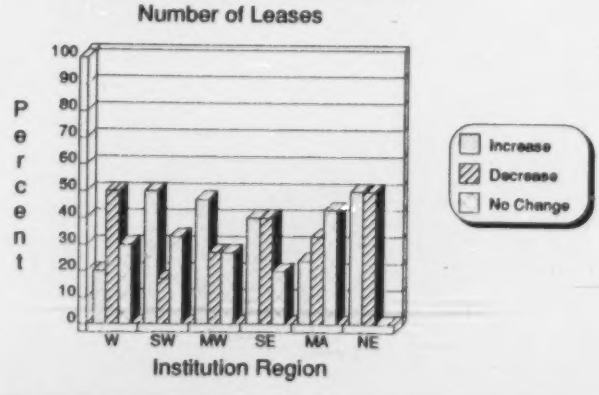


Figure 23



To assess the growth of the leasing industry in 1987 is difficult, given these mixed results. Overall, the results suggest that there has been an increase in leasing volume and the number of participants involved in automobile leasing. There appear to be differences in growth rate by institution size and region, but these numbers should be interpreted with caution. For those organizations that have recently entered leasing, the growth rate will be larger than for those who have been active for several years, due to starting from a smaller base.

The average value of the new car lease increased substantially from $15,969 in 1986 to $18,808 in 1987. Figures 24-25 illustrate 1987 total leasing volume by institution asset size:

Figure 24

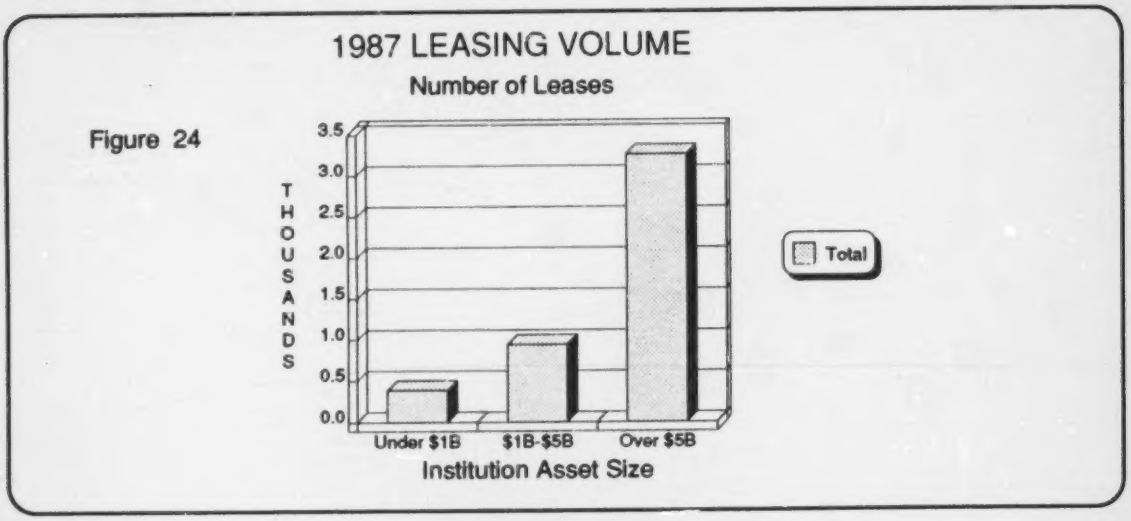
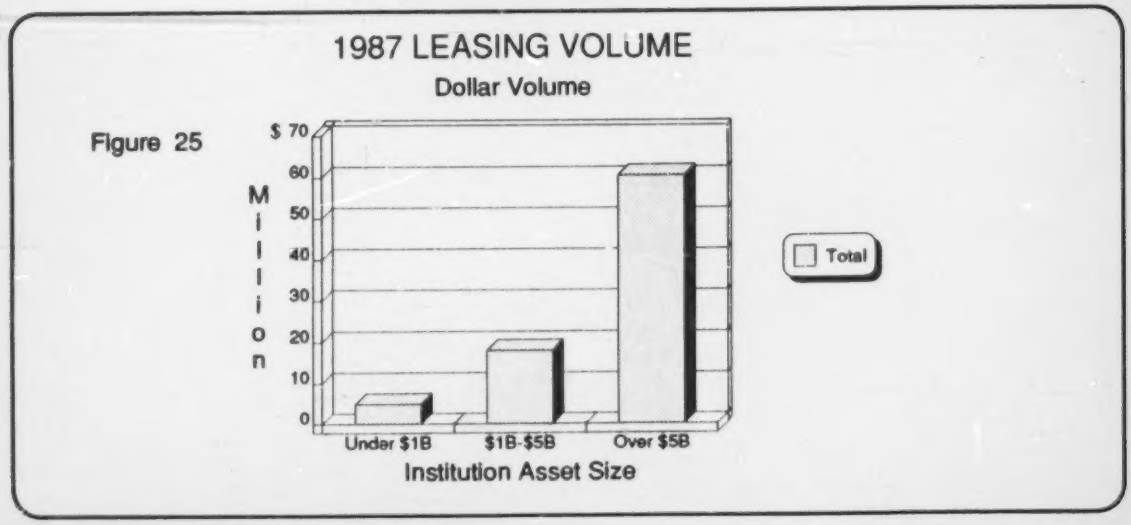


Figure 25



Leasing volume is strongly related to the size of the financial institution. Regionally, there are also differences in new car leasing volume, as highlighted in Table 6:

1987 AVERAGE LEASING VOLUME

Region	Vehicles	Volume	Average
West (W)	6026	$104.7	$17,272
Southwest (SW)	1330	$ 23.9	$17,964
Midwest (MW)	1383	$ 23.3	$16,841
Southeast (SE)	875	$ 19.3	$22,050
Mid-Atlantic (MA)	886	$ 36.4	$19,332
Northeast (NE)	1645	$ 42.1	$25,677

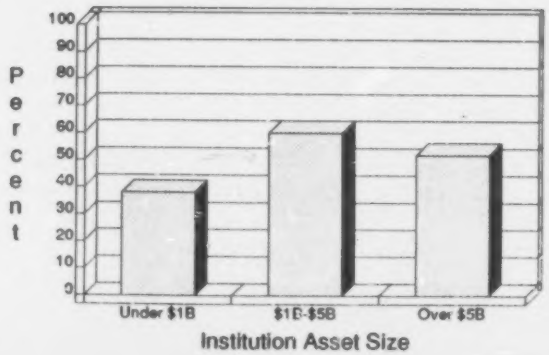
Table 6

Those organizations in the west (W) are clearly the leaders in leasing activity, although the southeast (SE) and northeast (NE) have substantially larger average leases. Closed-end leases comprised 94% of total lease activity in 1987. There were no apparent size differences in the percentage of closed-end leases. Regionally, however, the southeast (SE) was lower, with 81% of lease activity in closed-end leases.

The leasing of used cars is a service being offered by a growing number of financial institutions. In 1985, 37% of respondents offered used car leasing, in 1986 the percentage increased to 41%, and in 1987 it rose to 52%, and comprised 4.5% of the lease portfolio for those offering used car leases. Figures 26-27 show the percentages of institutions offering leases for used cars:

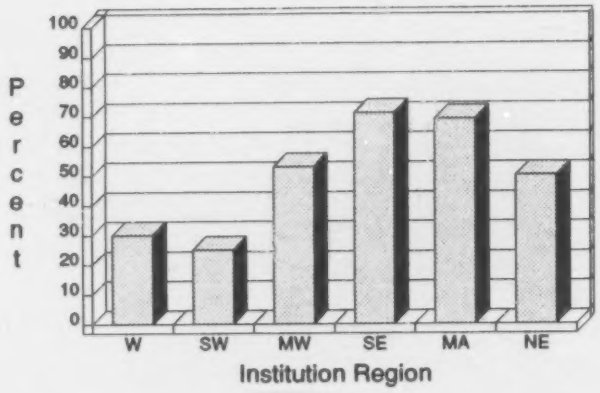
USED CAR LEASING

Figure 26



USED CAR LEASING

Figure 27



Institution size does not seem to be a major factor affecting used car leasing, but it appears as if those organizations in the western United States are not offering used car leases as commonly as those in the east.

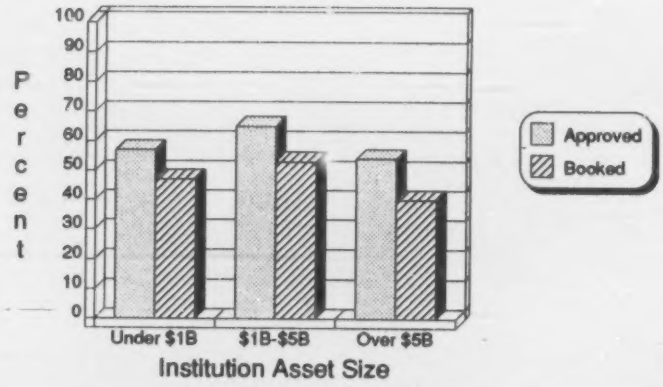
The mix of domestic and imported car leases has been an issue of major concern in the past and will continue to be in the future, particularly with the importance of residual value to the leasing program. Imported cars represented 45% of closed-end indirect leases and 43% of closed-end direct leases in 1987, virtually unchanged from 1986.

Lease Approval

In 1987 the average lease approval rate increased to 57% from 47% in 1986. Reasons may include a willingness to absorb a greater risk by approving a larger percentage of leases, excessive financing capacity, and writing a lease with a higher residual value. This may also reflect an increase in the number of affluent consumers who are considering leasing an automobile. The average lease approval percentages, as well as the percentages of leases booked are presented in Figures 28-29:

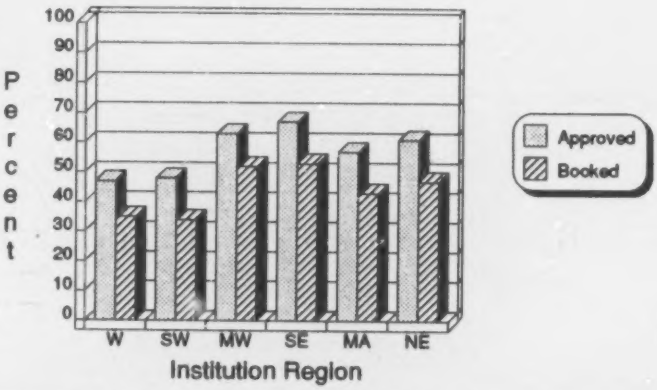
LEASE APPLICATIONS

Figure 28



LEASE APPLICATIONS

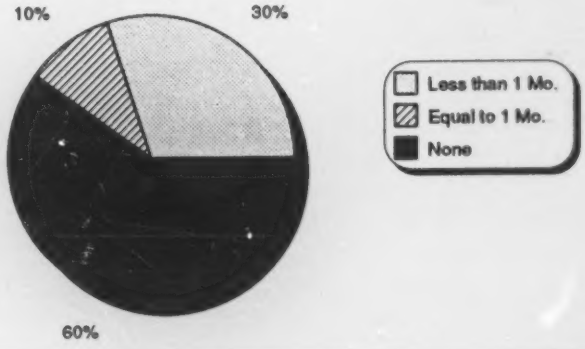
Figure 29



Lease approval rate varies by asset size, from 53% to 65%. Regionally, the approval rate is highest in the midwest (MW) and southeast (SE). The west (W) and southwest (SW) have a substantially lower rate of lease approval. The average of approved leases that were booked was 77%, and the average percentage of applications approved and booked was 44%. This figure provides an estimate of how efficiently an institution is obtaining the leases it approves. For example, institutions in the southwest (SW) convert 68% of their approved leases into actual leases. The use of a lease application fee and a substantial lease security deposit are becoming more common among those offering leasing services, as shown in Figures 30-31:

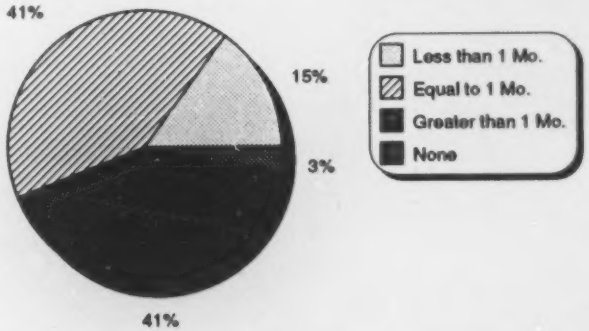
LEASE APPLICATION FEE

Figure 30



LEASE SECURITY DEPOSIT

Figure 31

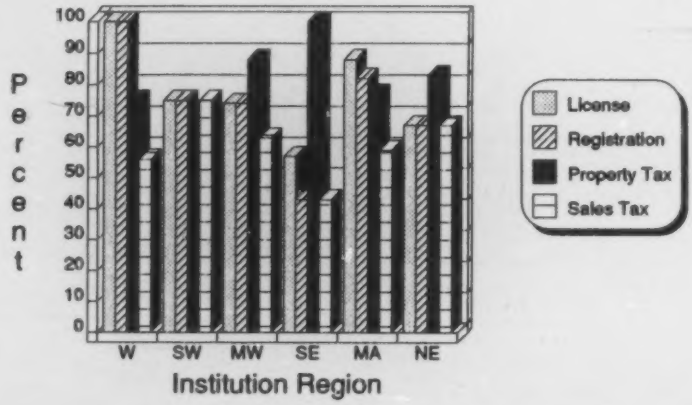


Overall, 40% of financial institutions now require a lease application fee, compared to 25% in 1986, and 97% require a security deposit.

Many financial institutions are capitalizing fees and taxes rather than passing them on directly to the lessee. The percentages of institutions capitalizing the various fees and taxes are presented in Figure 32:

CAPITALIZATION OF FEES & TAXES

Figure 32



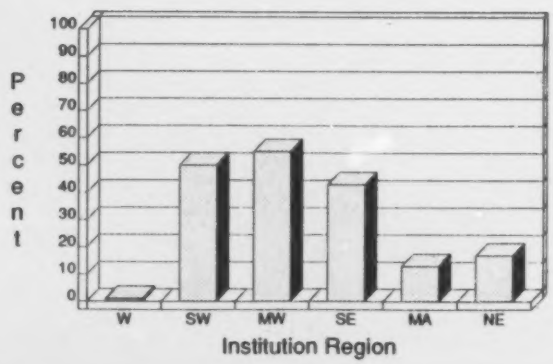
There were no size differences apparent in the results, however, regional differences were observed. For example, in the west (W) license and registration fees are typically capitalized, but this is done by less than 55% of the organizations in the southeast (SE).

In addition, 79% of all respondents capitalize dealer warranty packages.

The survey asked if an institution offered insurance as part of a lease arrangement. The number of financial institutions offering insurance has grown dramatically, from 0% in 1983 to 30% in 1987, and there are significant regional differences shown in Figure 33:

INSURANCE

Figure 33



In the west (W), there were no organizations offering insurance as part of the lease arrangement, while in the midwest (MW), it was offered by 55% of respondents. Of those offering insurance, 85% offered residual value insurance, and the average premium per lease was 1.4% of capitalized cost. Credit life and lease life were each offered by 3% of respondents. Almost 30% of respondents purchased residual value insurance with deductibles, and the average claim submitted under residual value insurance policies was $1,447 in 1987.

There are two primary means of lease payment collection - the use of coupon books and monthly billing. The use of these two methods varies substantially by institution asset size and geographic region, as shown in Figures 34-35:

Figure 34

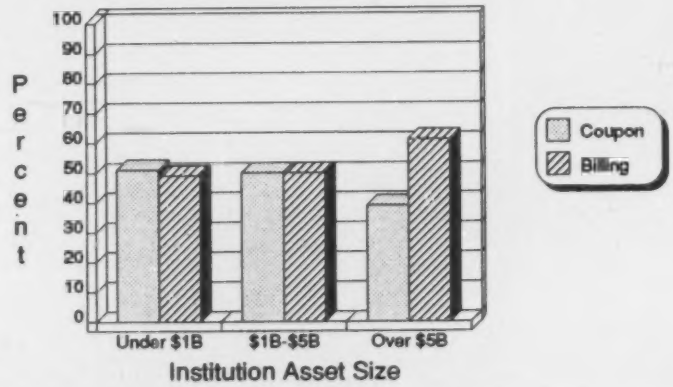
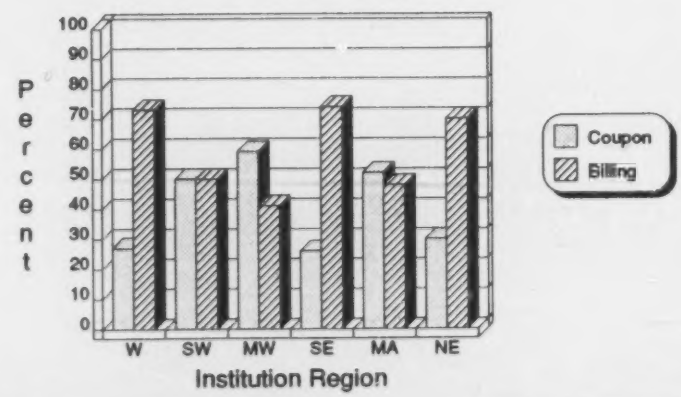


Figure 35

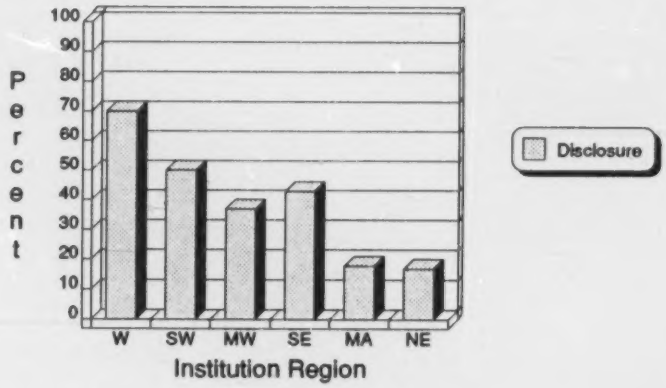


Over 60% of institutions with assets in excess of $5 Billion use monthly billing compared to 50% for smaller institutions. Regionally, institutions in the west (W), southwest (SW), and northeast (NE) prefer to use monthly billing, while those in the midwest (MW) favor coupon books.

Disclosure requirements are an emerging consumer issue in most areas of consumer banking. Only 37% of respondents disclose the capital cost of their leases, but there are substantial regional differences in disclosure, as illustrated in Figure 36:

LEASING CAPITALIZATION

Figure 36

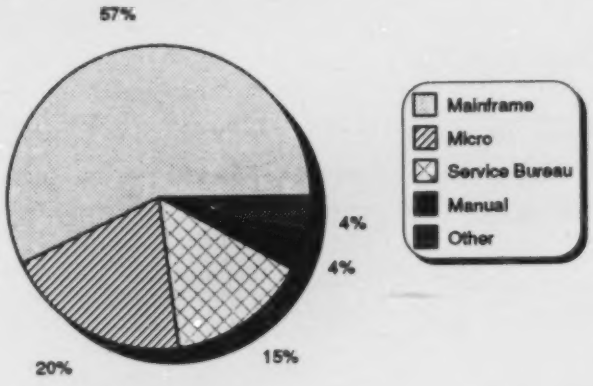


The percentage of institutions disclosing capital costs ranges from a low of 17% in the northeast (NE) to 70% of those institutions in the west (W). The average maximum capitalized cost, as a percentage of manufacturers' suggested retail price, was 103.4% for domestic cars and 106.2% for import cars.

Computerization is having a significant impact on the financing of automobiles, as lease application processing time, portfolio management, and the maintenance of stable dealer relationships becomes increasingly important. Figure 37 provides an illustration of the auto lease processing systems in use:

LEASE PROCESSING SYSTEM

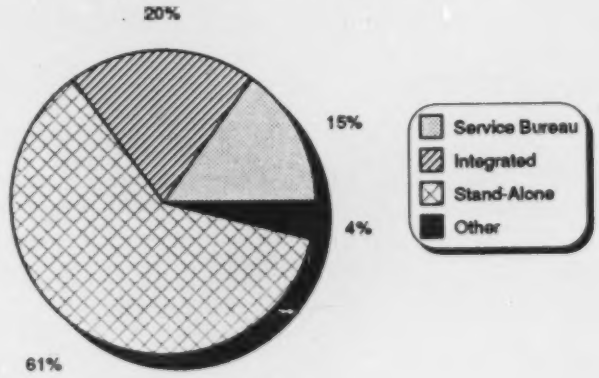
Figure 37



It is clear that the use of computers is crucial to the processing of leases for most organizations, as only 4% of respondents continue to rely on a manual system. The use of a mainframe or micro computer is the most common type of lease processing system. The auto leasing EDP system most commonly used is a stand-alone system serving the leasing function only, as illustrated in Figure 38:

LEASING EDP SYSTEM

Figure 38

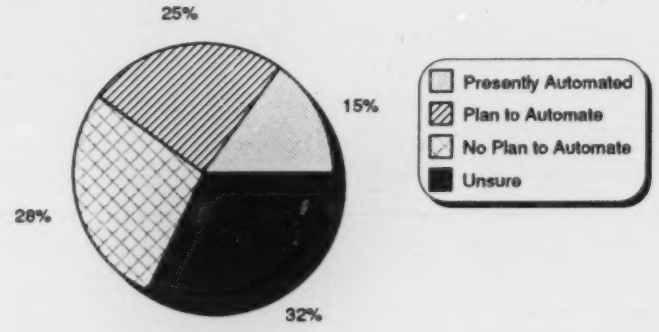


The use of a an EDP system that is integrated with other processing systems, such as consumer loans or auto credit, is used by 20% of respondents.

There has been significant progress made by the captive finance companies toward automating their relationships with franchised automobile dealers. This issue has generated a considerable degree of uncertainty among the survey respondents, as illustrated in Figure 39:

DEALER RELATIONSHIPS
STATUS OF AUTOMATION

Figure 39

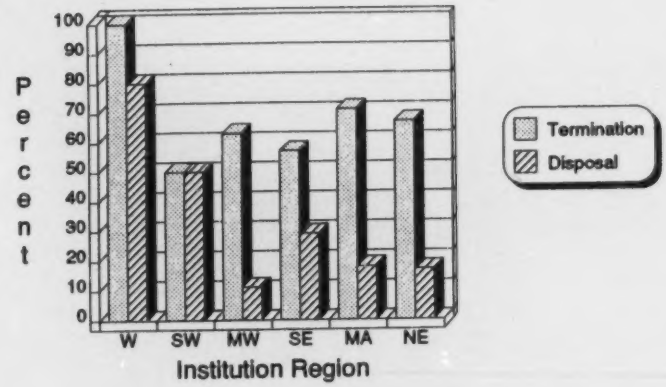


To date, 15% of respondents who offer leasing have automated relationships with dealers, while another 25% are planning to automate within the next two years. Almost one third of respondents were unsure of their plans, while 28% had no plans to automate.

With regard to the termination of leases, 77% of respondents allowed third party assumptions of original lease contracts, an increase of 7% from 1986. The average transaction fee was $230.00. When asked what percentage of leases terminated prior to maturity, respondents indicated that 27% did so in 1987, showing no change from 1986. Only 3% of leases terminated prior to the first year. Termination and disposal fees are commonly used by some financial institutions, as shown in Figure 40:

TERMINATION & DISPOSAL FEES

Figure 40

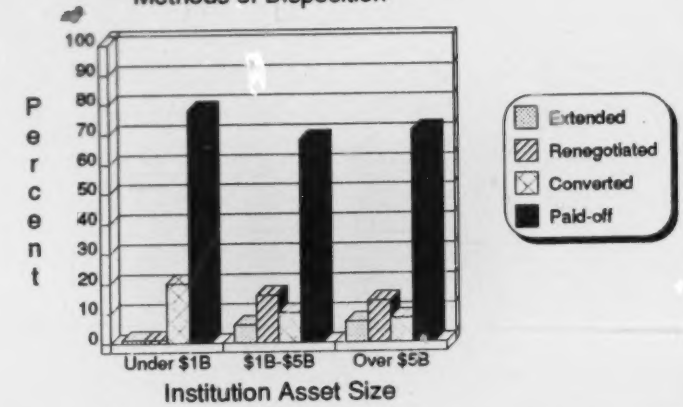


A termination fee was applied by 69% of respondents for early terminations, and averaged $165.00. Only 29% of respondents apply a disposal fee at lease maturity, with an average fee of $175.00. Organizations in the west (W) reported frequent use of both types of fees. For those lessees who maintained a lease to term, 76% expressed a willingness to allow an extension of the existing lease, compared to 66% in 1986. For leases reaching term, an average of 6% were extended month-to-month, 13% were renegotiated to a new lease, 10% were converted into a loan, but the vast majority were paid off for cash, as illustrated in Figure 41:

LEASES REACHING TERM

Methods of Disposition

Figure 41



Credit Quality

The average loss provision in 1987 was 1.3% of average net outstandings, compared to 1.10% in 1986, and .85% in 1984. The average actual loss was 1.18%, an increase from .93% in 1986, and .47% in 1984. This increase may reflect an increase in the competitiveness of the market.

The average percentage of lease delinquencies was lower than the 2.46% recorded in 1986. Lease payments 31 to 59 days overdue were 1.62% of total leases outstanding, and were relatively consistent across institution size and geographic region. The average for loans 60 to 89 days was 1.16%, and more than 90 days overdue was .97%. Figures 42-43 illustrates the percentages for closed-end leases by institution asset size and geographic region:

Figure 42

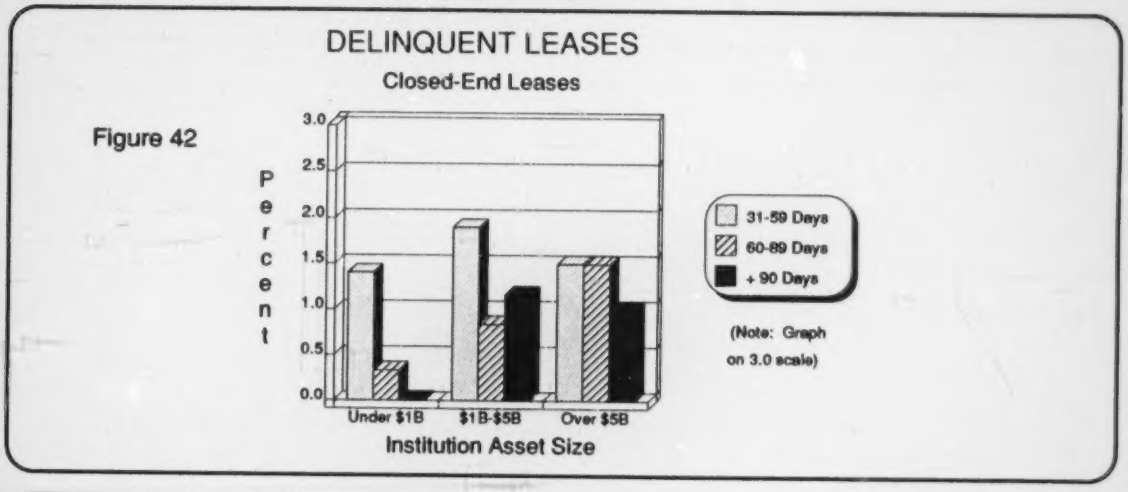
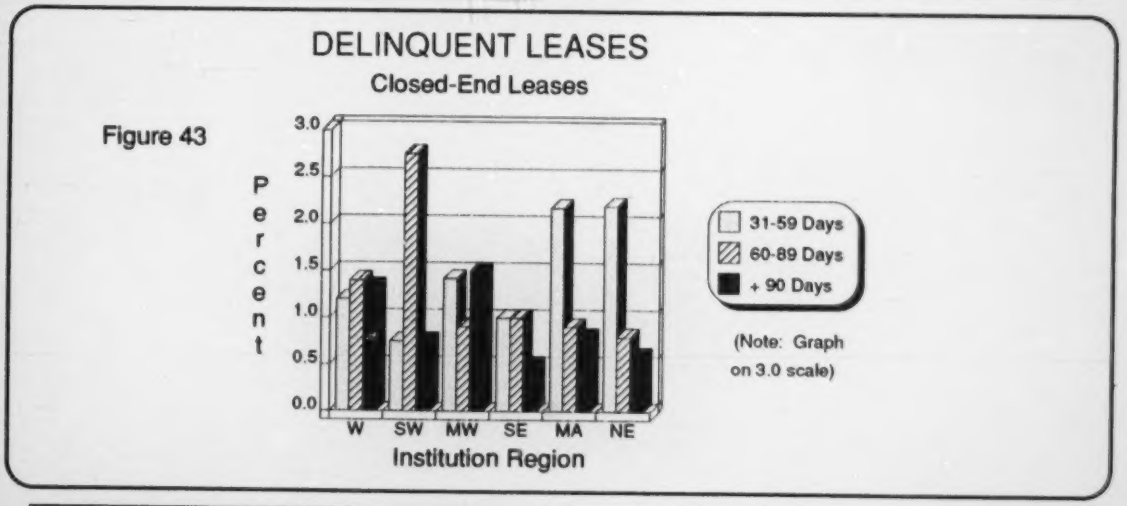


Figure 43



The institutions with assets of less than $1 Billion had a slightly lower overall delinquency rate. The only exceptions to the averages regionally were in the mid-atlantic (MA) and northeast (NE), where accounts delinquent 31 to 59 days exceeded 2.0%.

Repossessions averaged 228 vehicles per institution, with an average value loss per lease of $4,714. A breakdown of repossessions by region is provided in Table 7:

1987 AVERAGE LEASING REPOSSESSIONS

Region	Repossessions	Avg. Loss
West (W)	449	$3,800
Southwest (SW)	145	$4,359
Midwest (MW)	90	$5,665
Southeast (SE)	140	$3,563
Mid-Atlantic (MA)	259	$4,521
Northeast (NE)	316	$4,870

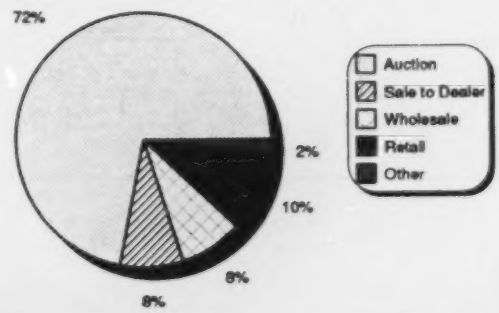
Table 7

Institutions with assets of less than $1 Billion averaged 137 repossessions while those between $1 Billion and $5 Billion averaged 158 and those in excess of $5 Billion averaged 276.

Automobiles that are repossessed must be disposed of in some manner, and there are a variety of ways of doing so, including a public or private auction, sale to a dealer, wholesaling, retailing, or other means, including retaining the vehicle for company use. Figure 44 provide a breakdown of the methods of disposal of repossessed vehicles:

DISPOSITION OF REPOSSESSIONS

Figure 44



All financial institutions clearly favor the use of an auction for vehicle disposal, as no size or regional differences were apparent in the survey responses.

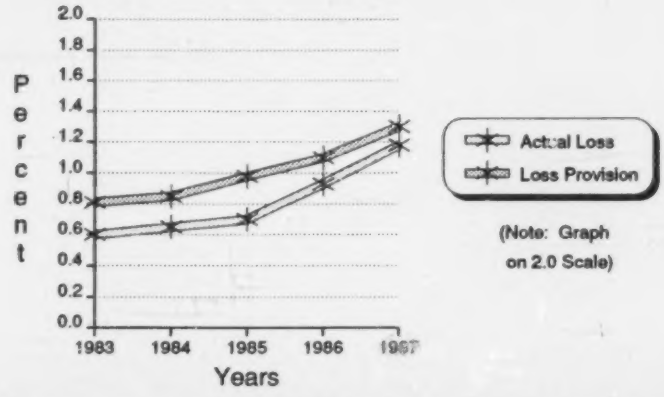
Conclusion

In summary, 1987 was a very good year for some leasing businesses, and a poor year for others. It would appear as if the potential for growth exists, yet there is a vast difference in the leasing success rates of financial organizations. Size seems to be a major factor in leasing, as the larger institutions have disproportionately larger leasing portfolios, and the west (W) remains the leader in leasing activity. Closed-end leases are becoming the norm, as 94% of new car leases were closed-end in 1987. Used car leasing is becoming more popular, now offered by over 50% of lessors.

There are two trends that have developed over the past several years which should be pointed out. First is the consistent increase in losses as a percentage of average net outstanding leases, as depicted in Figure 45:

LOSS PROVISION & ACTUAL LOSSES

Figure 45



Loss provisions have climbed from .80% of average net outstandings in 1983 to 1.3% in 1987. These figures do not correspond with loan approval rate or delinquencies, which have fluctuated up and down in recent years. This number should be interpreted with caution, however, as only 31% of respondents provided this information, and over half of those were institutions with assets in excess of $5 Billion. As the market for automobile leases changes, the risk involved with leasing will also change.

The second major trend is the dramatic rise in the capital cost of the average lease. In 1983, the average was $12,630, and since that time has risen to $18,808 as shown in Figure 46:

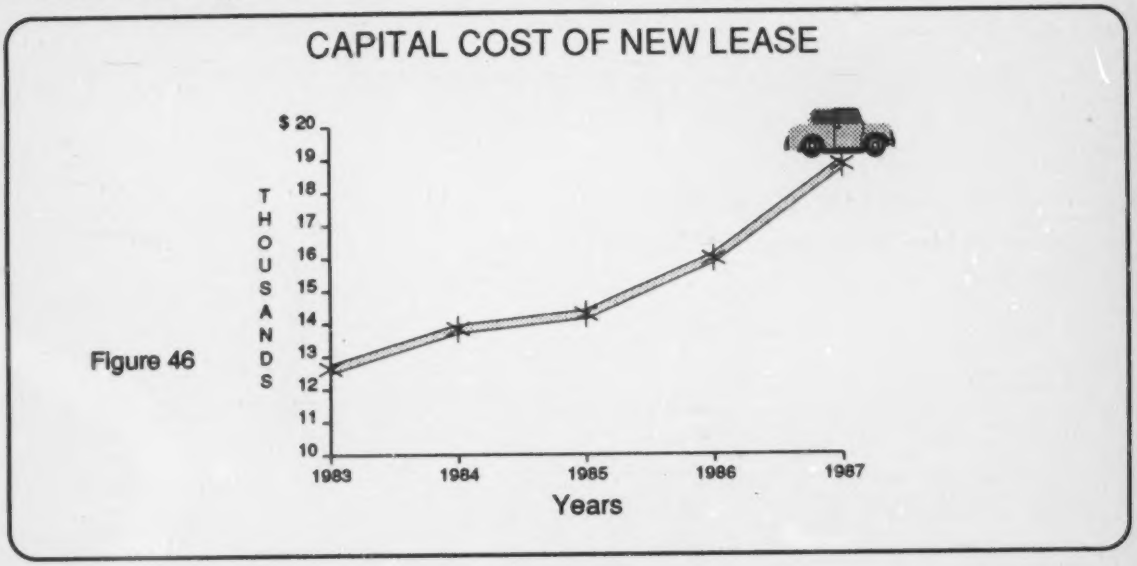


Figure 46

This could be the reflection of several factors, including changes in the tax laws, and eliminating consumer write-off of auto loan interest. However, it is clear that the trend toward leasing more expensive automobiles is continuing.

Automobile Financing

The Loan Portfolio

There were 159 financial institutions responding to the survey that offered automobile loans. The average loan portfolio consisted of 30,217 units financed at a value of $195 Million, and varied considerably by institution size and geographic region and is presented in Figures 47-50.

Figure 47

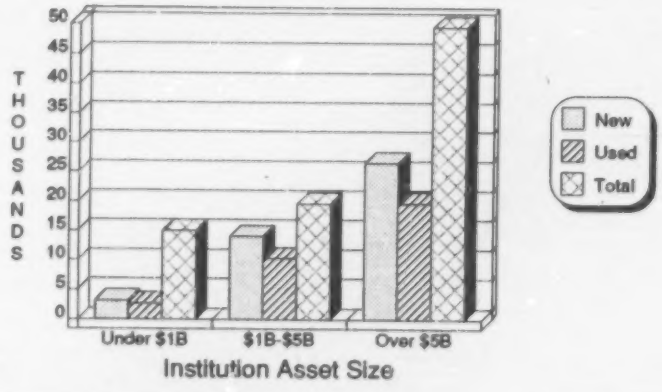


Figure 48

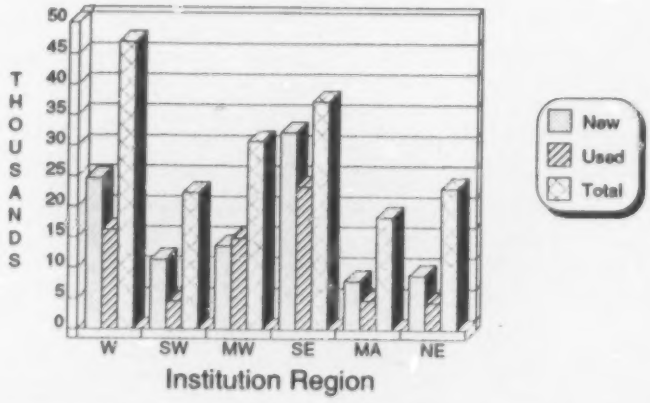


Figure 49

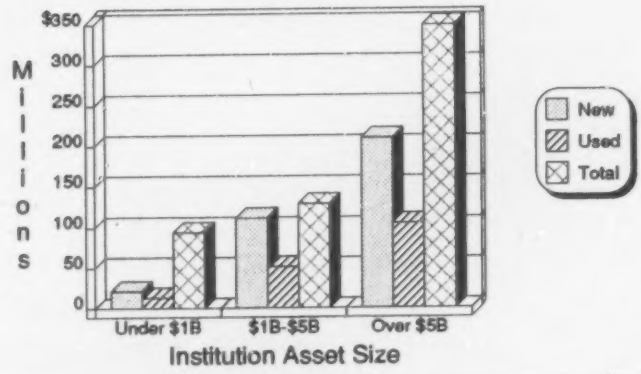
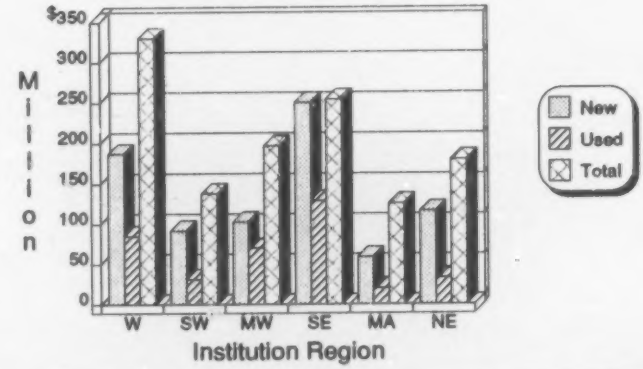


Figure 50



It is clear that as the institution size increases, the total number of loans also increases. Regionally, those institutions in the west (W), southeast (SE) and midwest (MW) tend to have more lending activity than the other regions. Averages ranged from a high in the west (W) of 46,918 total loans with $331 Million outstandings to a low of 18,298 total loans with $126 Million outstandings in the mid-atlantic (MA) region. The overall average value per loan was $7,732 for new cars, $5,236 for used cars, and $6,757 for the total portfolio outstandings, which increased from $6,460 in 1986. In terms of the mix of new and used cars in the portfolio, those institutions with assets of less than $1 Billion had 54% new car loans, while the larger institutions had 58%. Regionally, the west (W) had 60% new car loans, the southwest (SW) 72%, the midwest (MW) 42%, the southeast (SE) 58%, the mid-Atlantic (MA) 63%, and the northeast (NE) 67%.

Employees

The 1987 survey contained items pertaining to the number of employees involved in the lending function, as well as the salaries for these employees. Figures 51-53 present the results of the survey:

Figure 51

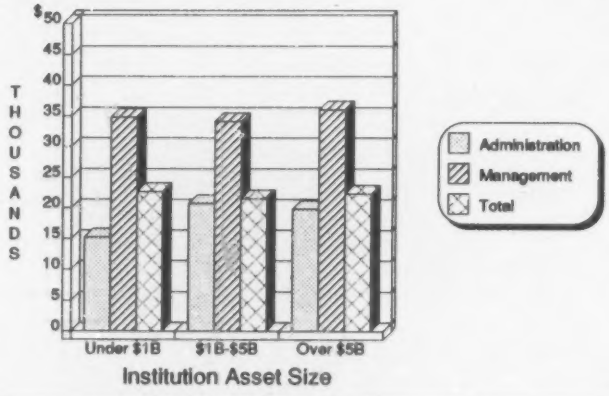
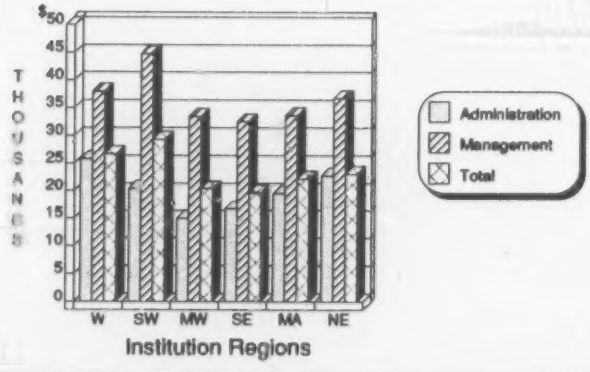
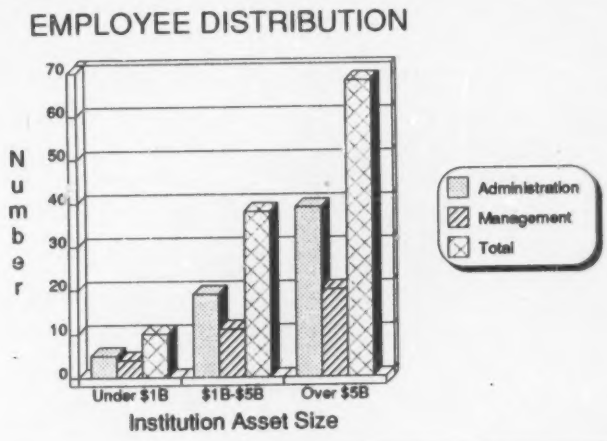


Figure 52



As expected, the larger institutions employ more individuals, but the ratio of managerial employees to administrative personnel decreases with size. Over 36% of the number of total employees are classified as managers (exempt) for those institutions with assets of less than $1 Billion, while 28% are classified as managers by the larger institutions. Salaries vary little by institution asset size, but do show some regional differences, with higher average salaries in the west (W), southwest (SW), and northeast (NE).

Figure 53



Lending Activity

The optimism expressed in the 1986 survey regarding expectations for 1987 was justified for many lending institutions. There was, however, a great deal of difference among the performance of lending institutions in 1987, as 52% of respondents reported an increase in lending volume, while 48% reported a decrease. This is consistent with the figures from 1986, when 51% of respondents reported an increase in lending activity.

For those who gained, the average increase in the number of loans was 29%, while the average dollar volume increase was 42%. The number of new car loans averaged an increase of 24% with a range from 9% to 60%. Dollar volume increased an average of 27% with a range from 13% to 44%. The number of used car loans increased 17% ranging from 1% to 47%, while dollar volume increased 24% with a range of 7% to 56%. The greatest increase was experienced by those institutions with assets of less than $1 Billion.

For those institutions reporting a decrease, this average was -19% for the number of loans and -12% for dollar volume. The number of new car loans showed a decrease of -12% ranging from -10% to -33%. New car loan dollar volume decreased -9% with a range of -6% to -36%. The number of new car loans decreased 26% with a range from -20% to -34%. The dollar volume of used car loans decreased -25% ranging from -18% to -33%. Those institutions with assets in excess of $5 Billion experienced the greatest reductions.

Overall, there was a 4.5% increase in the number of new car loans, and a decrease of -7% in used car loans. The dollar volume of new car loans increased 7%, and used cars 3%. The volume of indirect loans increased at a rate twice that of direct loans. The changes in total loan activity are presented in Figures 54-57, using 1.0 as the baseline. Thus, percentages of less than one for 1987 represent decreases in the portfolio while those greater than one are increases.

Figure 54

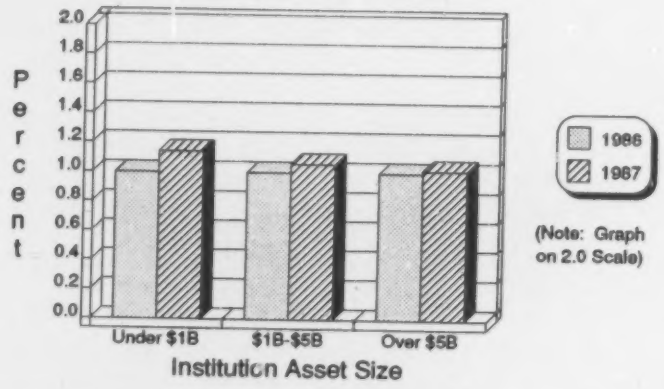
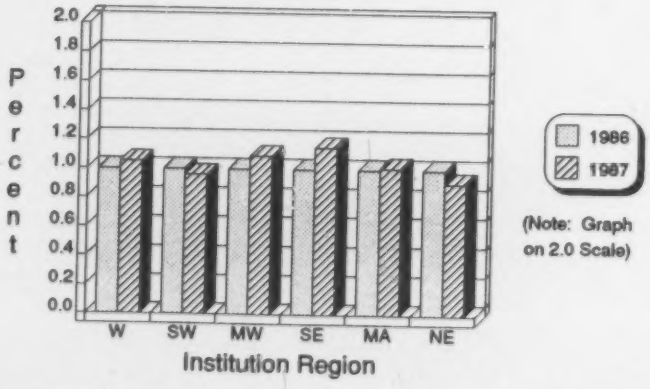


Figure 55

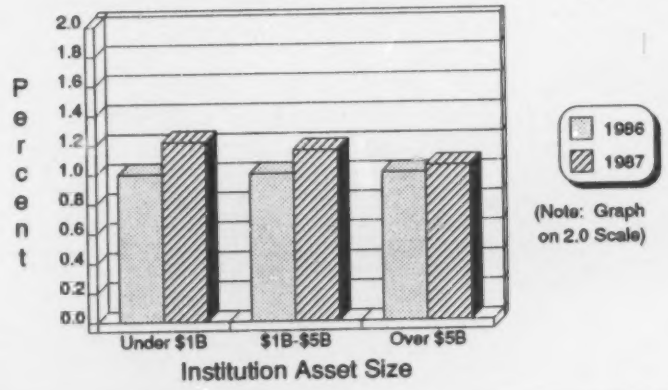


Those institutions with assets of less than $1 Billion experienced the greatest increase in their portfolios, with an average increase of 14% in the number of loans and a 22% increase in dollar volume. It is important to keep in mind, however, that percentage increases are more easily obtained when starting from a smaller base.

LOAN PORTFOLIO

1986-1987 Dollar Volume Outstandings

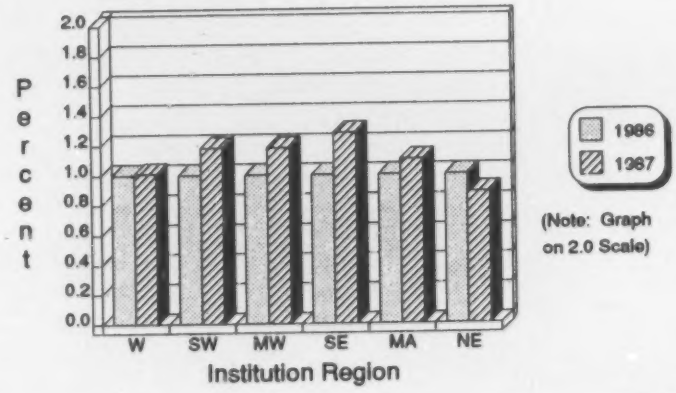
Figure 56



LOAN PORTFOLIO

1986-1987 Dollar Outstandings

Figure 57



All regions of the country with the exception of the southwest (SW) and northeast (NE) experienced an increase in the number of loans, and all except the northeast increased the dollar volume of loans.

The average portfolio turnover was 31 months and the average new loan turnover 36 months, unchanged from 1986. The average term for a new car loan increased to 53 months from 50 months in 1986, and the average maximum maturity was 58 months.

The mix of domestic and imported car loans has been an issue of major concern in the past and will continue to be in the future. In 1986 the percentage of car loans for new imports increased to 48% from 45% in 1985. The average percentage in 1987 was 45%, a slight decrease from 1986. The average percentage of loans for used imports in 1987 was 36%. Overall, there has been little significant change in the portfolio mix of domestic and imported cars reported in the last several years. Figures 58-61 provide an illustration of the types of loans by institution asset size and geographic region.

Figure 58

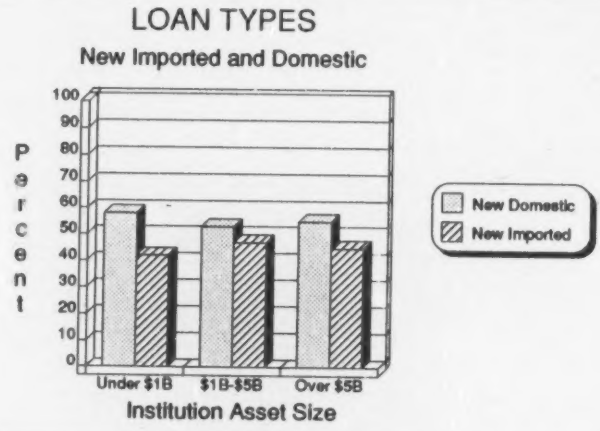


Figure 59

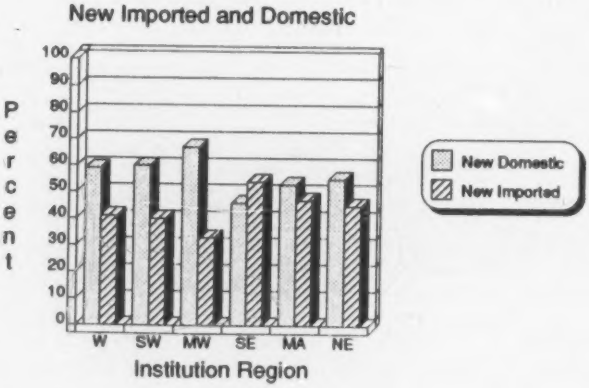


Figure 60

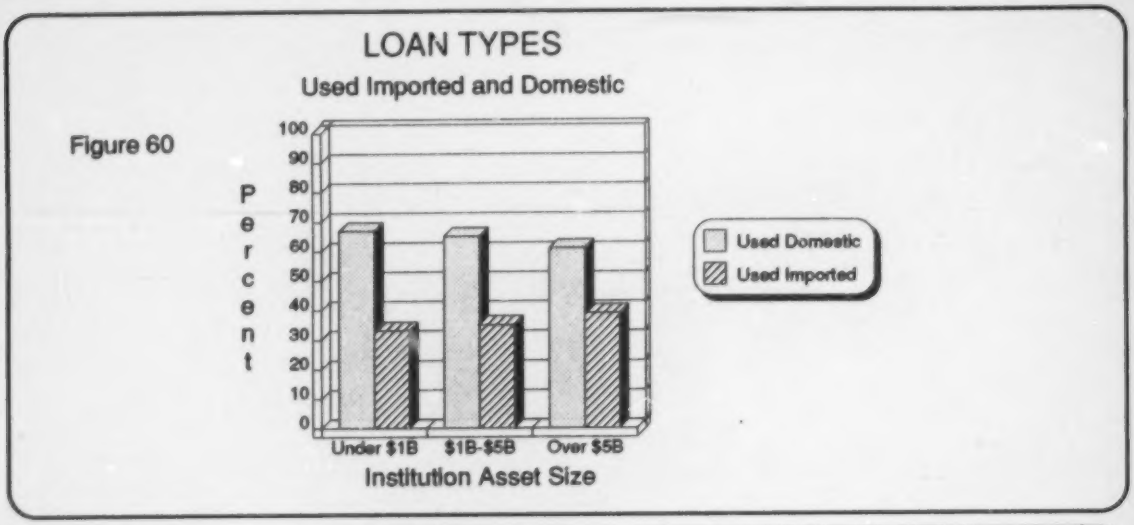
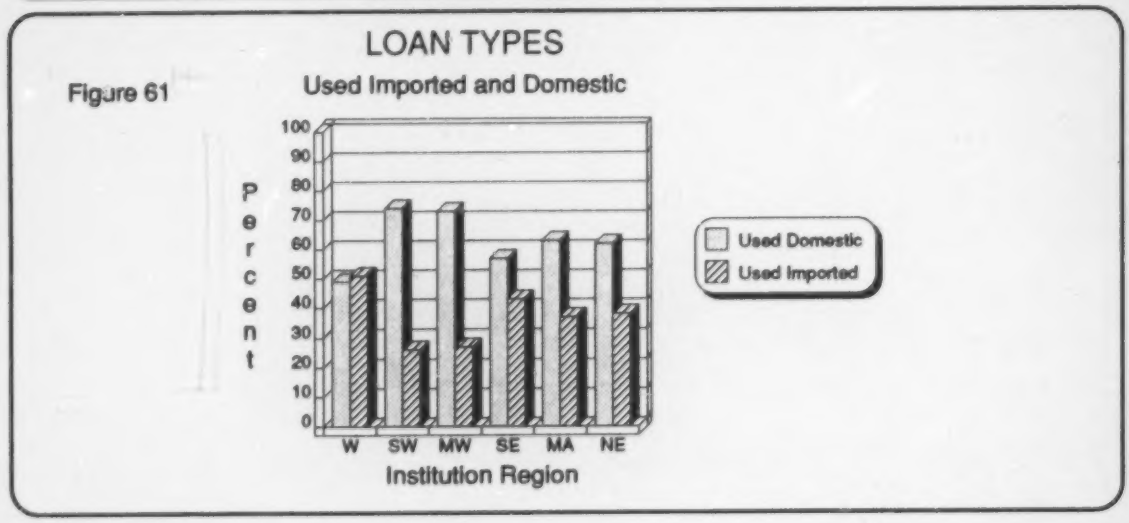


Figure 61

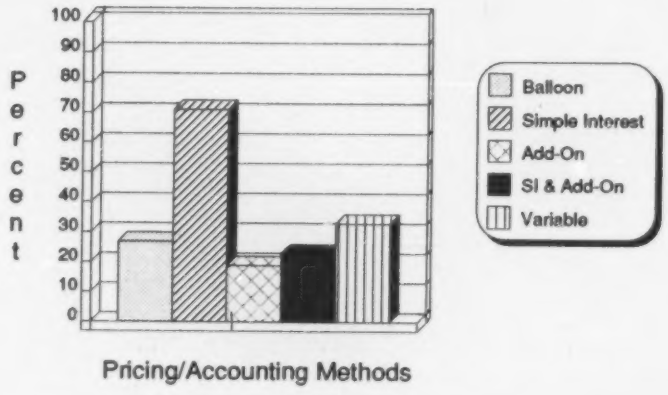


Those institutions with assets of less than $1 Billion tended to make a greater percentage of their loans for domestic automobiles, with 58% of their new car loans and 67% of their used car loans for domestic cars. Regionally, the percentage of loans made for new imported cars increases in the eastern part of the country, led by the southeast (SE), with 56% of new car loans being made for imports. This may reflect growth in the east and a saturation of the import car market in the western United States. Loans for used cars are dominated by domestic automobiles in all regions of the country except the west, where 47% of used car loans were for imports. The average downpayment for new cars was 13%, and 16% for used cars.

There are a variety of pricing/accounting methods being employed by lending institutions. The percentages of institutions using the various methods are presented for the entire sample in Figure 62:

PRICING/ACCOUNTING METHODS

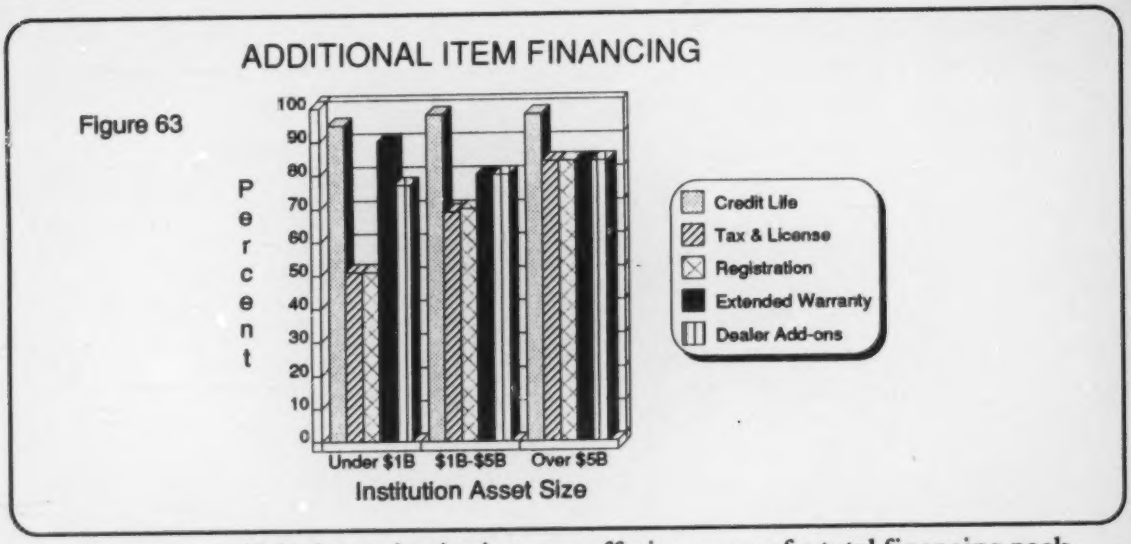
Figure 62



There was a substantial amount of agreement across size and region of these methods, as all lending institutions used them in approximately the same proportions. Simple interest is the method offered by over 70% of lending institutions, although variable rate car loans are offered by over one third of the respondents. Institutions with assets less than $5 Billion offered balloon notes more frequently, 30% compared to 21% of institutions with asssets in excess of $5 Billion. For those organizations offering a balloon payment program, an average of 2.7% of new dollar volume is tied to the program.

Many lending institutions are offering financing for items in addition to the automobile. These include credit life insurance, tax and license, registration fee, extended warranties, and dealer added accessories. No regional differences emerged in the use of these practices, but institutions of different sizes vary somewhat in their offerings. Figure 63 illustrates the percentage of institutions offering the various additional item financing:

Figure 63

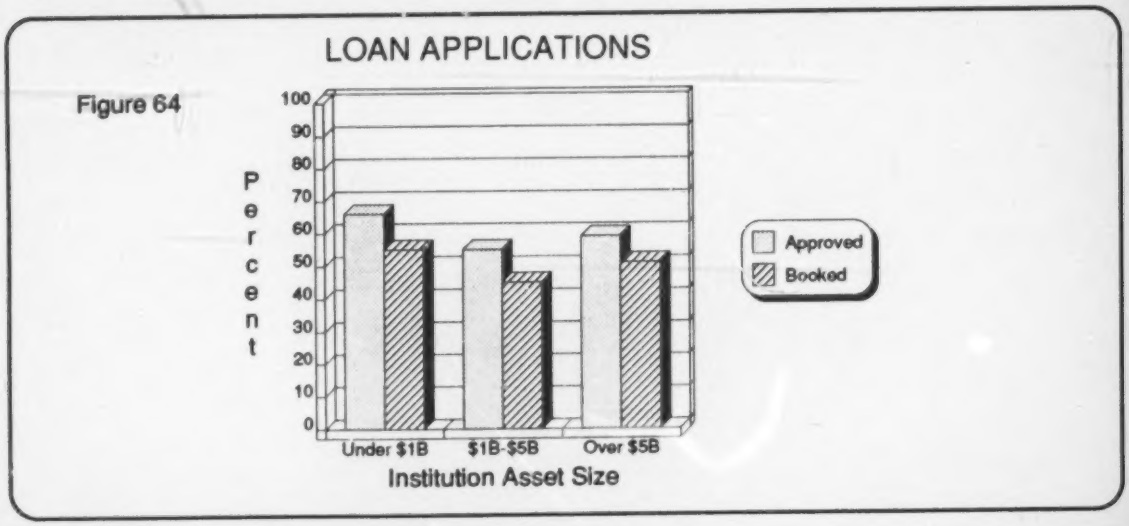


It appears as if the larger institutions are offering more of a total financing package to the consumer, possibly making the purchase of an automobile more convenient for the dealership and the consumer.

Loan Approval

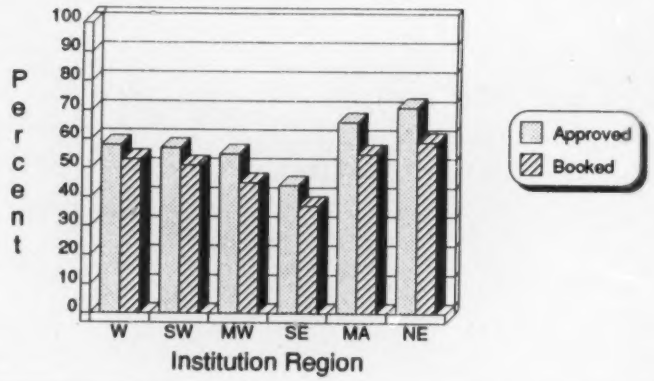
In 1986 the average loan approval rate increased to 69% from 61% in 1985, reflecting either a possible willingness to assume greater risk, higher quality applicants, or an appetite for assets. In 1987, the average loan approval rate decreased to a more conservative 59%. The average loan approval percentages, as well as the percentages of loans booked are presented in Figures 64-65:

Figure 64



LOAN APPLICATIONS

Figure 65



Loan approval rate varies by asset size, from 65% for those institutions with assets of less than $1 Billion to 55% for those between $l Billion and $5 Billion. Regionally, the approval rate is highest in the mid-Atlantic (MA) and northeast (NE) regions, and lowest in the southeast (SE). The average of approved loans that were booked was 80% and the average percentage of loan applications approved and booked was 49%.

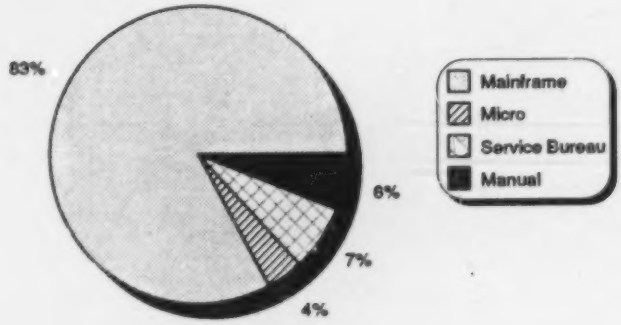
Credit scoring is used by 29% of the overall sample, the same percentage as in 1986. There are significant differences among the various organization sizes, as credit scoring is used by only 16% of the institutions with assets of less than $1 Billion, 28% of those between $1 Billion and $5 Billion, and 39% of those over $5 Billion.

Computerization

Computerization is having a significant impact on the financing of automobiles, as loan processing time and the maintenance of stable dealer relationships becomes increasingly important. Figure 66 provides an illustration of the auto lending processing systems in use:

LOAN PROCESSING SYSTEM

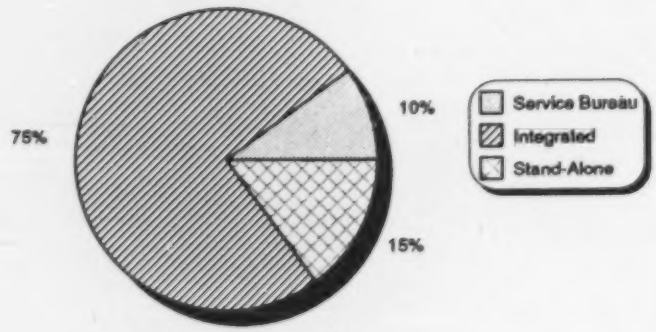
Figure 66



It is clear that the use of computers is crucial to the processing of loans, for most organizations, as only 6% of respondents continue to rely on a manual system. The auto lending EDP system is most commonly integrated with other processing systems such as DDA, consumer loans, or CIF, as illustrated in Figure 67:

LENDING EDP SYSTEM

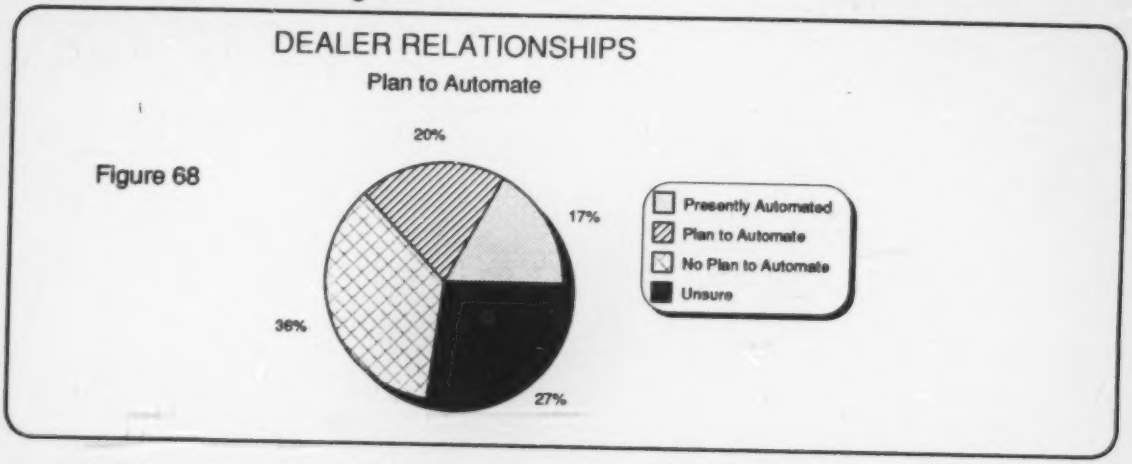
Figure 67



The use of a stand-alone system serving the auto lending function only is becoming more common, however, as reported by 15% of the survey respondents.

There has been significant progress made by the captive finance companies toward automating their relationships with franchised automobile dealers. This issue has generated a considerable degree of uncertainty among the survey respondents, as illustrated in Figure 68:

Figure 68

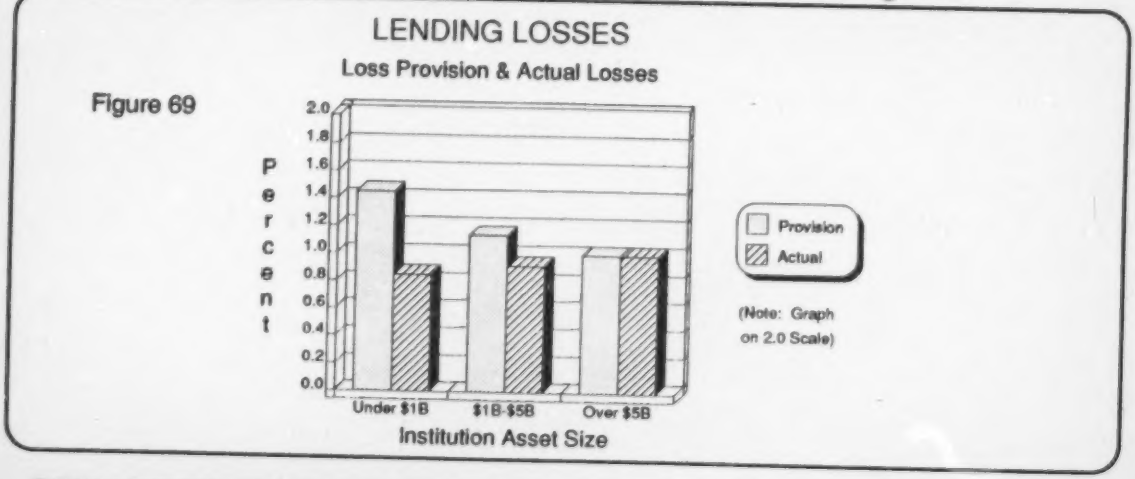


To date, 17% of respondents have automated relationships with dealers, while another 20% are planning to automate within the next two years. Almost one third of respondents have no plans to automate, while over 25% of respondents were usure of their plans.

Credit Quality

The average loss provision in 1987 was 1.2% of average net outstandings, compared to 1.10% in 1986. The average actual loss was .92%, a decrease of .18% from 1986. The percentages by institution asset size are presented in Figure 69:

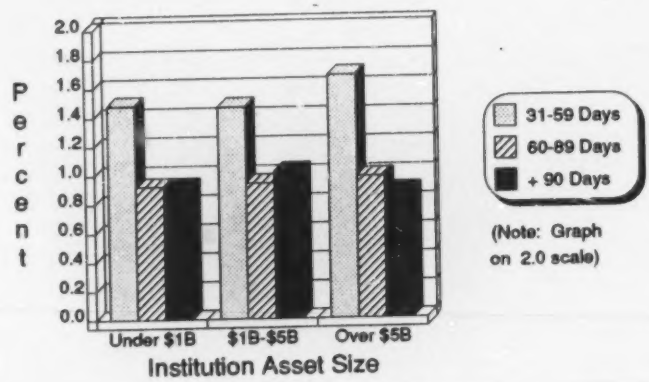
Figure 69



The average percentage of loan delinquencies 31 to 59 days overdue for 1987 were lower than the previous year, down to 1.55% of total loans outstanding from 1.88%, and were relatively consistent across institution size and geographic region. The average for loans 60 to 89 days and more than 90 days overdue was .95%. There was no difference in delinquencies between direct and indirect loans. Figure 70 illustrates the percentages by institution asset size:

DELINQUENT LOANS

Figure 70



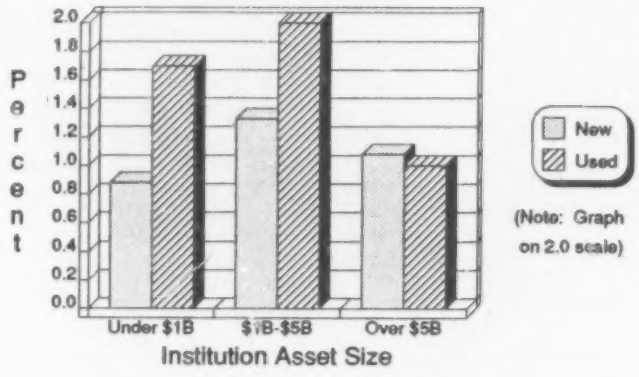
The largest institutions had a slightly higher rate at 1.68% for loans 31 to 59 days overdue. The only exception to the averages regionally was in the midwest (MW) which had 1.31% of loans overdue more than 90 days, .36 greater than the overall average.

The number of automobile repossessions appears to have increased from 1986 to 1987. Repossessions of new cars resulted in a loss of 1.1% of average net dollar outstandings in 1987, compared to .76% in 1986. Losses generated by used car repossessions also climbed significantly from .90% in 1986 to 1.52% in 1987. This increase may have resulted from the increased loan approval rate in 1986. Figure 71 illustrates losses generated by repossessions as a percentage of total net dollar outstandings by institution asset size.

AUTOMOBILE REPOSSESSIONS

New and Used

Figure 71

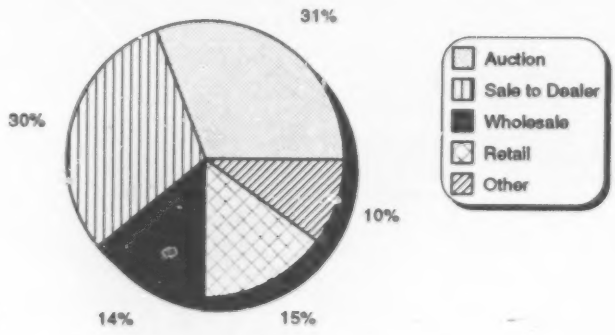


Automobiles that are repossessed must be disposed of in some manner, and there are a variety of ways of doing so, including a public or private auction, sale to a dealer, wholesaling, retailing, or other means, including retaining the vehicle for company use. Figures 72-74 provide a breakdown of the methods of disposal by institution asset size:

DISPOSAL OF REPOSSESSIONS

Institution Asset Size Under $1B

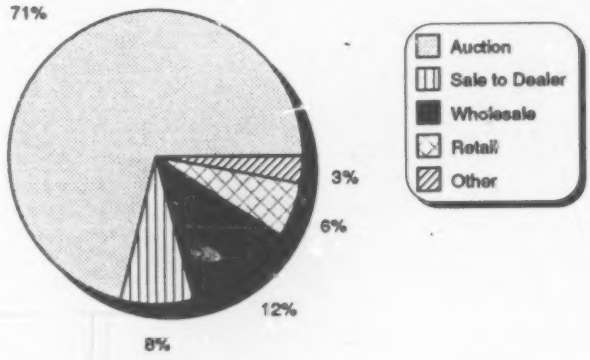
Figure 72



DISPOSAL OF REPOSSESSION

Institution Asset Size $1B-$5B

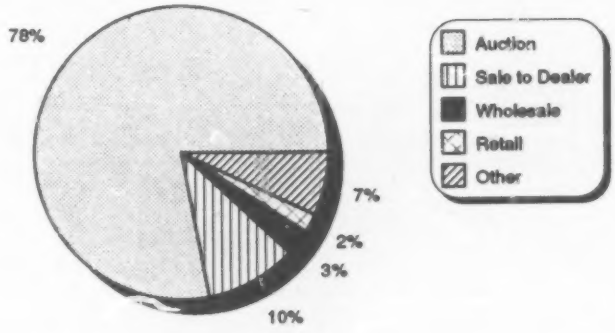
Figure 73



DISPOSAL OF REPOSSESSIONS

Institution Asset Size Over $5B

Figure 74



The larger institutions clearly favor the use of an auction for vehicle disposal, while those institutions with assets less than $1 Billion utilize a variety of methods. There were no regional differences apparent in the survey responses.

Conclusion

Overall, the modest increase in loan volume for 1987 may reflect some success in dealing with the captive finance companies. Imported car loans have been approaching 50% of the average lending portfolio in recent years, yet imported car sales comprised only one third of total new car sales for 1987. This suggests that banks and thrifts are doing more financing of imports while the captives are focusing on the financing of domestic cars. The decrease in used car loans may have been caused by an increase in the number of inexpensive cars in the marketplace.

There have been no major changes in loan approval rate, delinquencies, or lending terms, yet some financial institutions fared quite well in 1987. Regionally, some of that difference may be a reflection of the condition of local economies, but much of the success must be attributed to more effective marketing of the product. Automobile financing is becoming a mature industry, and, as such, organizations must recognize that efficiency and cost management are going to become increasingly important. In the future, facing increased competition, organizations are also going to have to become more responsive to their customers, both auto dealerships and the purchaser.

Automobile Floorplanning

Automobile wholesale financing activities comprise a major portion of the lending portfolio for many financial institutions. Floorplanning services were offered by 70% of this years's respondents, compared to 66% for 1986. All financed 100% of the manufacturer's invoice for new units. In 1987, the number of wholesale units that became retail loans was 31%, compared to 27% in 1986 and 35% in 1985. The number of automobiles in an average floorplan portfolio was 3,854, and the dollar volume $46.2 Million. Figures 75-78 provide an illustration of floorplan financing by institution asset size and geographical region:

Figure 75

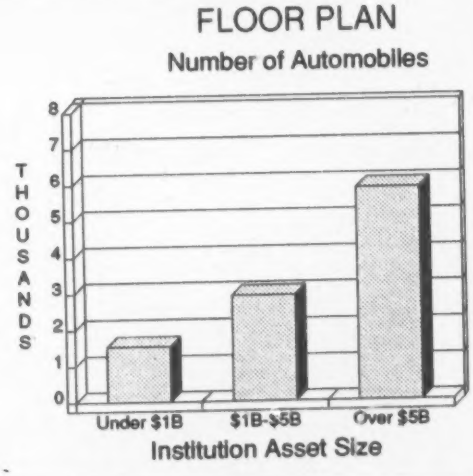


Figure 76

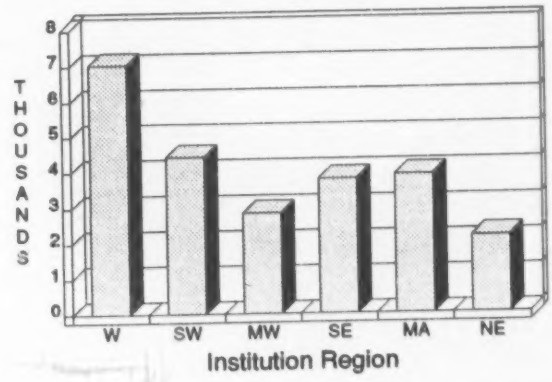


Figure 77

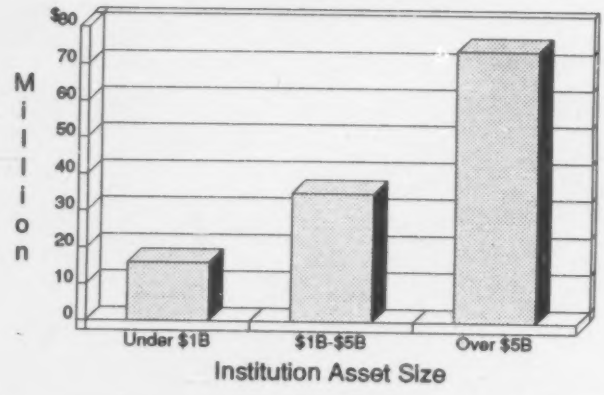
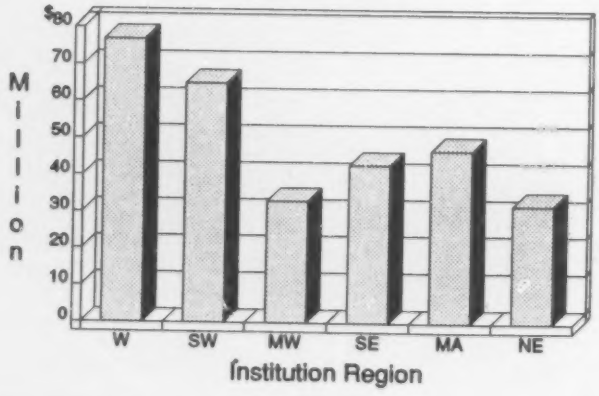


Figure 78

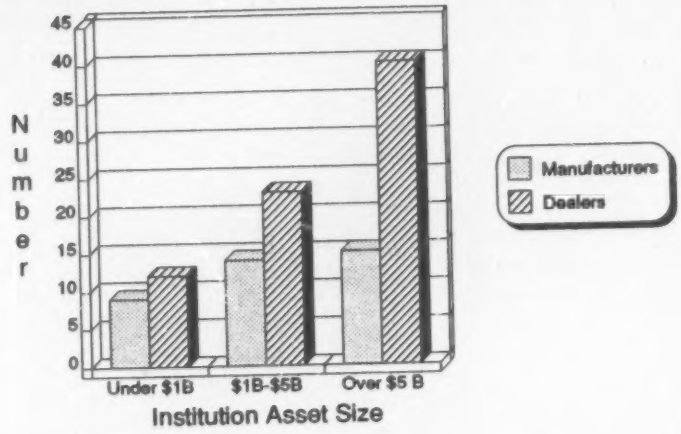


It is clear that floorplan financing is related to institution asset size as those with assets in excess of $5 Billion had an average of 5,866 automobiles in their portfolio compared to 1,540 for those with assets of less than $1 Billion. Regionally, institutions in the west (W) and southwest (SW) appear to be the most active in wholesale financing activities. The floorplan financing of used vehicles was offered by 76% of those who provide wholesale financing services, with an average of 206 used automobiles in the portfolio.

The number of manufacturing firms represented in an average portfolio was 13.5, and did not vary significantly by region or by size. The average number of dealership floorplanning relationships was 26, and there was a substantial regional difference in the number of relationships maintained by financial institutions. These relationships are presented in Figures 79-80:

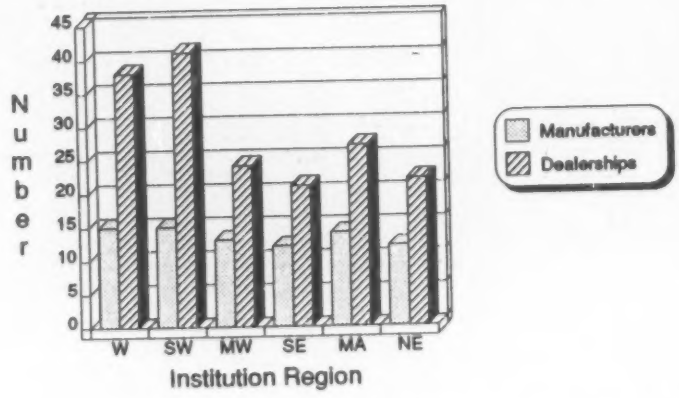
MANUFACTURERS & DEALERSHIPS

Figure 79



MANUFACTURERS & DEALERSHIPS

Figure 80



Once again regional differences suggest that those institutions in the west (W) and southwest (SW) are most active with regard to floor planning activity, as they generate the most dollar volume and maintain the most dealer relationships. Also of interest is the average number of units financed, the dollar outstandings, and the average unit value per dealer relationship. These are presented by region in Table 8:

AVERAGE INDIVIDUAL DEALERSHIP RELATIONSHIPS

Region	Units	Outstandings	Average
West (W)	124	$1,472,178	$11,872
Southwest (SW)	126	$1,996,376	$15,844
Midwest (MW)	117	$1,162,012	$ 9,931
Southeast (SE)	144	$1,599,858	$11,110
Mid-Atlantic (MA)	135	$1,664,951	$12,332
Northeast (NE)	78	$1,105,840	$14,177

Table 8

These numbers illustrate that although floorplan total outstandings for institutions in the west (W) and southwest (SW) is much larger than that for the rest of the country, the average number of vehicles per dealership does not always follow this pattern. Also highlighted is the large per unit value differences by region, with the midwest (MW) the lowest and the southwest (SW) the highest. Overall, the average dollar volume per dealership was $1.5 Million, down from an average of $1.9 Million in 1986.

Floorplan Protection

There are a variety of methods that are used by lending institutions to protect the floorplan portfolio. The frequency of use for each method is presented in Figures 81-86 by geographic region:

Figure 81

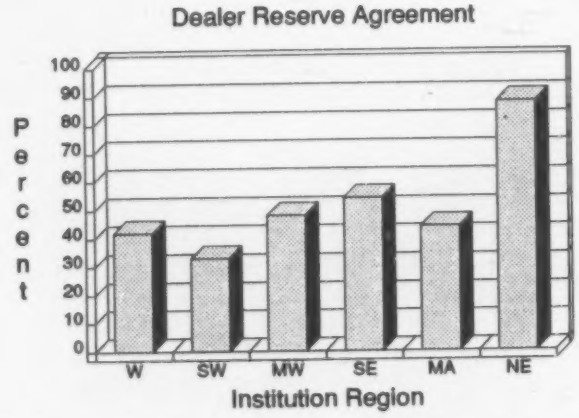
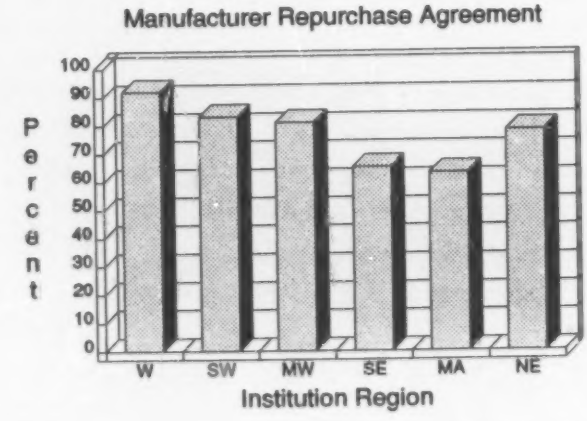


Figure 82



The use of the dealer reserve agreement varies substantially from 32% of institutions in the southwest (SW) to 88% in the northeast (NE). The manufacturer repurchase agreement is commonly used by institution in all regions of the country.

Figure 83

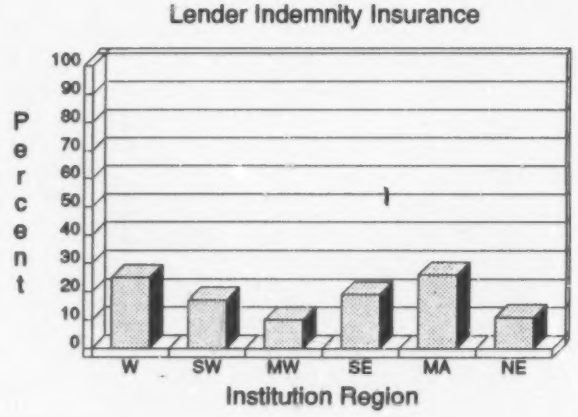
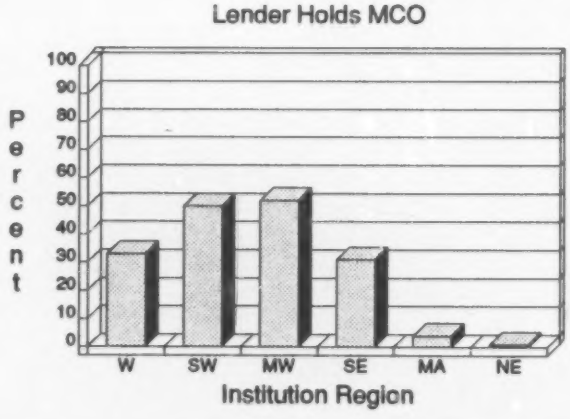


Figure 84



Lender indemnity insurance is not commonly used by respondents in any region, ranging from a low of 10% in the midwest (MW) to a high of 25% in the mid-atlantic region (MA). One major difference that emerged in floorplan protection is in the retaining of the manufacturer's certificate of origination (MCO), which is done by 52% of institutions in the midwest (MW) but is very seldom done in the mid-atlantic (MA) or northeastern (NE) regions. No differences in the use of the various types of floorplan protection were apparent among the different sizes of institutions with the exception of the MCO, which is retained by 61% of institutions with assets of less than $1 Billion and only 20% of the larger institutions.

Figure 85

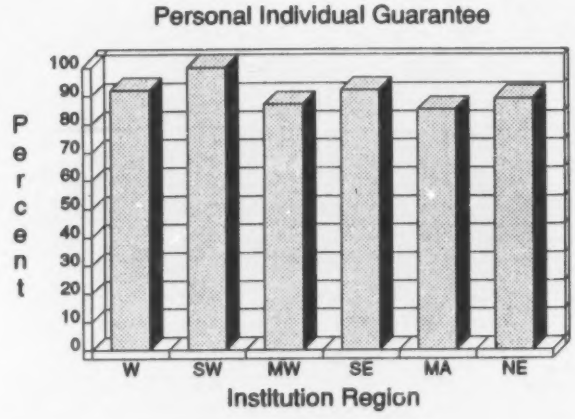


Figure 86

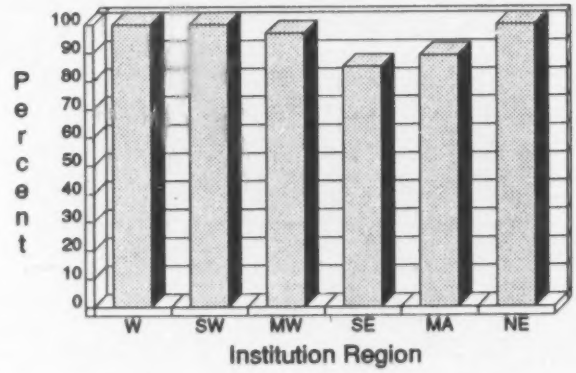
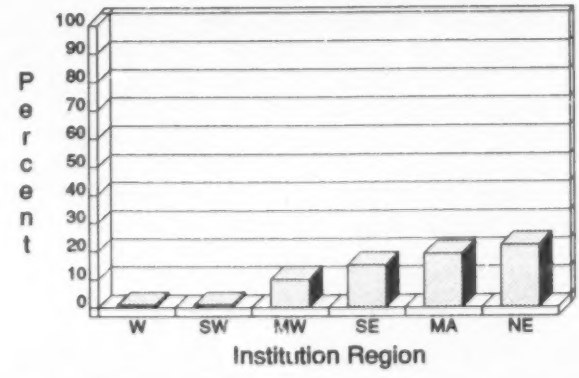


Figure 87



The use of a personal individual guarantee and the inspection and verification of floorplanned units by in-house personnel are the most commonly used methods of protection, while verification of floorplanned units by a service company is least favored. Many financial institutions use two or more of the various types of floorplan protection, depending on regional regulations and relationship with the dealer.

The 1987 survey attempted to identify the most commonly used renewal (curtailment) terms that financial institutions employ in their dealer relationships. The results suggest that there are a very large variety of renewal terms that are affected by type of vehicle, new versus used cars, credit history of dealer, interest rates, size of dealership, and many other factors. The primary conclusion that can be drawn is that there is no standard renewal term, and each lending institution tailors the terms to its needs and to the needs of the individual dealership.

Conclusion

Floorplan activity will vary directly with new automobile sales volume. One area of growth in floorplanning is in used cars, as an increasing number of institutions are now offering used car floorplanning. The demand for used car floorplanning will also vary with new car sales, as those sales will result in an increased number of trade-ins that will need to be financed. With the increase in indirect lending activity and the growth in auto leasing, it is important for financial institutions to develop sound business relationships with dealerships. The floorplanning of vehicles, both new and used, is an effective means of doing so.

Due to the interest of CBA members, the Auto Finance Committee plans to expand the survey questionnaire to provide more information regarding floorplanning activity in 1988.

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